

China State Construction International

2014 NP +26%; net gearing at 36.8% at end 2014

2014 YoY: revenue +26%, ex-interest revenue/GP +26%/22% and NP +26%

2014 revenue rose 26% YoY to HK\$34.4bn, and gross profit improved 27% YoY to HK\$4.7bn. If we exclude the HK\$1.0bn interest income from BT projects, revenue and gross profit increased 26%/22% YoY respectively. Interest income jumped 45% YoY to HK\$1.2bn, and net profit rose 26% YoY to HK\$3.5bn, which is in-line with both our estimate and consensus estimate. A full year DPS of HK\$0.26 (30% payout) was declared, 24% higher than 2013 DPS of HK\$0.21, similar to our estimate.

Organic growth remains solid on existing business

We remain confident on the outlook for the existing business. Affordable housing new starts are expected to be 7.44m units (+6% YoY) in 2015, while relocation housing (i.e. Shanty Town Redevelopment, CSCI's addressable market) should show a more significant 23% YoY increase in 2015. Furthermore, CSCI management remains confident on expanding market share. In the HK market, we see some major infrastructure projects, e.g. the third runway of HK airport and Phase 2 of Disneyland. MGM's big casino new project built a high base in 2015, but we expect Macau's new contract will remain significant to reflect follow-up projects from MGM, as well as in Hengqin Island.

Asset injection provides another growth driver

We see asset injection as another future growth driver on top of organic growth. We think overseas construction businesses (e.g. Singapore and US) owned by the parent company are good potential asset injection targets, to follow the government's "One Road and One Belt" strategy. Management confirmed that the acquisition of Laizhou port and three warehouses a few months ago was the start of a series of M&A and asset injections.

Valuation: Buy rating, fine-tuning PT to HK\$14.50 (from HK\$15.00)

Our 12m price target of HK\$14.50 is based on 13.4x our 2015 EPS estimate of HK\$1.09.

Equities

China
Heavy Construction

12-month rating **Buy**

12m price target **HK\$14.50**
Prior: HK\$15.00

Price **HK\$10.64**

RIC: 3311.HK BBG: 3311 HK

Trading data and key metrics

52-wk range	HK\$14.08-10.62
Market cap.	HK\$41.4bn/US\$5.33bn
Shares o/s	3,887m (ORD)
Free float	37%
Avg. daily volume ('000)	6,698
Avg. daily value (m)	HK\$75.5
Common s/h equity (12/15E)	HK\$23.0bn
P/BV (12/15E)	1.9x
Net debt / EBITDA (12/15E)	2.8x

EPS (UBS, diluted) (HK\$)

	From	To	% ch	Cons.
12/15E	1.13	1.09	-3.83	1.12
12/16E	1.34	1.26	-6.41	1.39
12/17E	1.61	1.55	-3.88	-

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Highlights (HK\$m)	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
Revenues	21,626	26,611	33,434	40,402	45,665	53,961	63,361	74,076
EBIT (UBS)	1,694	2,029	2,705	3,920	4,542	5,459	6,453	7,573
Net earnings (UBS)	2,044	2,606	3,233	4,354	5,045	6,033	7,202	8,569
EPS (UBS, diluted) (HK\$)	0.54	0.66	0.82	1.09	1.26	1.55	1.80	2.14
DPS (HK\$)	0.16	0.21	0.26	0.34	0.39	0.47	0.56	0.66
Net (debt) / cash	(3,170)	(4,596)	(7,366)	(12,689)	(13,256)	(15,055)	(16,805)	(19,041)
Profitability/valuation	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
EBIT margin %	7.8	7.6	8.1	9.7	9.9	10.1	10.2	10.2
ROIC (EBIT) %	16.9	13.4	14.6	16.1	14.8	15.2	15.2	15.1
EV/EBITDA (core) x	11.4	16.4	10.9	4.8	4.1	3.2	2.5	1.8
P/E (UBS, diluted) x	14.5	18.0	15.6	9.8	8.5	6.9	5.9	5.0
Equity FCF (UBS) yield %	(11.9)	(7.4)	(0.5)	(12.4)	2.4	0.2	1.2	1.0
Net dividend yield %	2.0	1.8	2.0	3.2	3.7	4.4	5.2	6.2

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of HK\$10.64 on 20 Mar 2015 19:56 HKT

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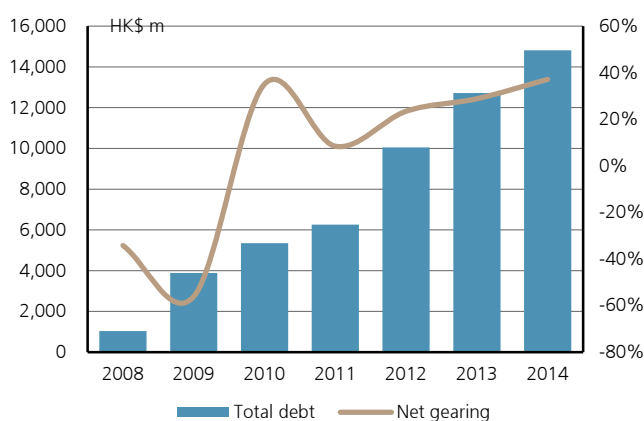
FY14 result review

Figure 1: P&L

	H113	H213	H114	H214	2013	2014	YoY
Revenue (HK\$ m)	11,267	15,250	13,784	19,650	26,517	33,434	26%
Gross profit (HK\$ m)	1,380	1,681	1,527	2,211	3,061	3,738	22%
<i>Gross margin</i>	12.2%	11.0%	11.1%	11.2%	11.5%	11.2%	
EBIT (HK\$ m)	906	1,138	1,105	1,600	2,044	2,705	33%
<i>EBIT margin</i>	8.0%	7.5%	8.0%	8.1%	7.7%	8.1%	
Net profit (HK\$ m)	1,173	1,599	1,465	1,992	2,772	3,457	26%
<i>Net margin</i>	10.4%	10.5%	10.6%	10.1%	10.5%	10.3%	
EPS (HK\$)	0.30	0.41	0.38	0.50	0.71	0.89	26%
DPS (HK\$)	0.09	0.12	0.11	0.15	0.21	0.26	24%

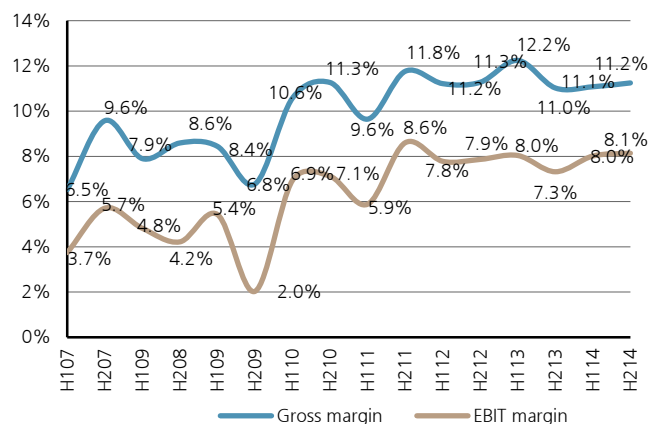
Source: Company data

Figure 2: Total debt and net gearing



Source: Company data

Figure 3: Gross margin and EBIT margin

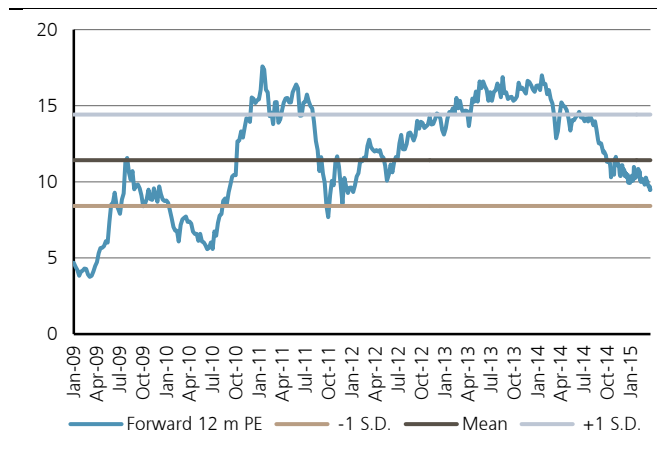


Note: both gross margin and EBIT margin calculation excluded interest income from BT projects; Source: Company data

Valuation and basis for our price target

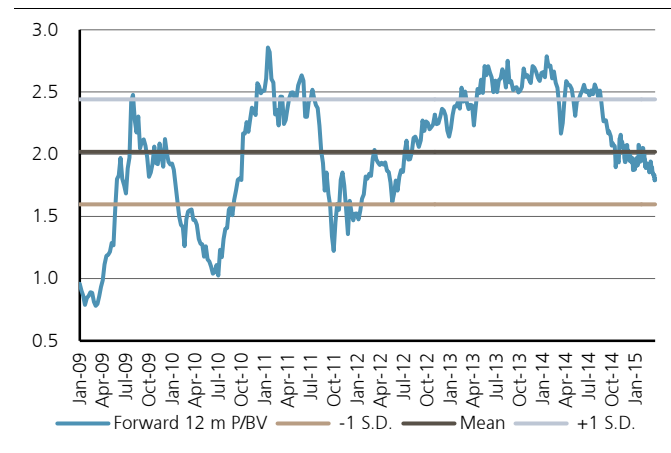
We fine-tuned our 12m PE-based price target from HK\$15.00 to HK\$14.50 to reflect earnings revisions and incorporation of new share issuance to purchase assets from the parent company. **PT of HK\$14.50**

Figure 4: 12-month forward PE



Source: Bloomberg, UBS estimates

Figure 5: 12-month forward P/BV



Source: Bloomberg, UBS estimates

China State Construction International (3311.HK)

Income statement (HK\$m)	12/12	12/13	12/14	12/15E	% ch	12/16E	% ch	12/17E	12/18E	12/19E
Revenues	21,626	26,611	33,434	40,402	20.8	45,665	13.0	53,961	63,361	74,076
Gross profit	2,434	3,071	3,738	5,169	38.3	5,931	14.7	7,073	8,316	9,714
EBITDA (UBS)	1,968	2,322	3,220	4,473	38.9	5,133	14.8	6,088	7,120	8,277
Depreciation & amortisation	(274)	(293)	(515)	(553)	7.3	(591)	6.8	(629)	(666)	(704)
EBIT (UBS)	1,694	2,029	2,705	3,920	44.9	4,542	15.9	5,459	6,453	7,573
Associates & investment income	602	547	347	368	6.0	387	5.2	407	429	451
Other non-operating income	24	39	19	19	0.0	19	0.0	19	19	19
Net interest	114	383	704	933	32.5	1,136	21.8	1,410	1,820	2,344
Exceptionals (incl goodwill)	108	176	272	272	0.0	272	0.0	272	272	272
Profit before tax	2,541	3,174	4,048	5,513	36.2	6,357	15.3	7,568	8,993	10,660
Tax	(405)	(503)	(660)	(921)	-39.5	(1,067)	-16.0	(1,279)	(1,529)	(1,822)
Profit after tax	2,137	2,671	3,388	4,592	35.5	5,290	15.2	6,288	7,464	8,838
Preference dividends and Minorities	(5)	79	70	(14)	-	(21)	-53.6	(31)	(37)	(44)
Extraordinary items	0	0	0	0	-	0	-	0	0	0
Net earnings (local GAAP)	2,131	2,750	3,457	4,578	32.4	5,268	15.1	6,257	7,426	8,793
Net earnings (UBS)	2,044	2,606	3,233	4,354	34.7	5,045	15.8	6,033	7,202	8,569
Tax rate (%)	15.9	15.9	16.3	16.7	2.4	16.8	0.6	16.9	17.0	17.1
Per share (HK\$)	12/12	12/13	12/14	12/15E	% ch	12/16E	% ch	12/17E	12/18E	12/19E
EPS (UBS, diluted)	0.54	0.66	0.82	1.09	32.6	1.26	15.8	1.55	1.80	2.14
EPS (local GAAP, diluted)	0.56	0.70	0.88	1.14	30.4	1.31	15.1	1.61	1.85	2.19
EPS (UBS, basic)	0.55	0.67	0.83	1.09	30.8	1.26	15.8	1.55	1.80	2.14
Net DPS (HK\$)	0.16	0.21	0.26	0.34	31.7	0.39	15.1	0.47	0.56	0.66
Book value per share	3.48	4.10	5.10	5.74	12.5	6.66	16.1	8.00	9.05	10.58
Average shares (diluted)	3,776.73	3,946.05	3,950.51	4,012.42	1.6	4,012.42	0.0	3,887.45	4,012.42	4,012.42
Balance sheet (HK\$m)	12/12	12/13	12/14	12/15E	% ch	12/16E	% ch	12/17E	12/18E	12/19E
Cash and equivalents	6,875	8,126	7,452	5,130	-31.2	6,553	27.7	6,764	5,014	2,778
Other current assets	14,289	20,927	26,877	30,162	12.2	33,416	10.8	38,350	44,175	51,065
Total current assets	21,164	29,053	34,330	35,292	2.8	39,969	13.3	45,115	49,188	53,843
Net tangible fixed assets	2,191	2,672	2,827	2,998	6.1	3,270	9.1	3,503	3,699	3,857
Net intangible fixed assets	6,332	7,158	7,309	6,648	-9.0	6,393	-3.8	6,138	5,883	5,628
Investments / other assets	8,147	13,567	22,113	25,625	15.9	28,697	12.0	33,342	38,845	45,378
Total assets	37,835	52,450	66,579	70,564	6.0	78,329	11.0	88,098	97,616	108,707
Trade payables & other ST liabilities	13,048	22,500	30,634	28,400	-7.3	30,456	7.2	33,814	38,096	42,988
Short term debt	49	262	587	587	0.0	587	0.0	587	587	587
Total current liabilities	13,097	22,761	31,221	28,987	-7.2	31,043	7.1	34,401	38,684	43,575
Long term debt	9,996	12,461	14,232	17,232	21.1	19,222	11.6	21,232	21,232	21,232
Other long term liabilities	888	1,041	1,129	1,129	0.0	1,129	0.0	1,129	1,129	1,129
Preferred shares	0	0	0	0	-	0	-	0	0	0
Total liabilities (incl pref shares)	23,982	36,263	46,581	47,347	1.6	51,394	8.5	56,762	61,044	65,935
Common s/h equity	13,510	15,934	19,830	23,035	16.2	26,732	16.1	31,102	36,301	42,456
Minority interests	343	253	168	181	8.2	203	11.7	234	271	315
Total liabilities & equity	37,835	52,450	66,579	70,564	6.0	78,329	11.0	88,098	97,616	108,707
Cash flow (HK\$m)	12/12	12/13	12/14	12/15E	% ch	12/16E	% ch	12/17E	12/18E	12/19E
Net income (before pref divs)	2,131	2,750	3,457	4,578	32.4	5,268	15.1	6,257	7,426	8,793
Depreciation & amortisation	274	293	515	553	7.3	591	6.8	629	666	704
Net change in working capital	(5,426)	(6,297)	(3,539)	(9,682)	-173.6	(4,277)	55.8	(6,229)	(7,053)	(8,540)
Other operating	(74)	143	(70)	14	-	21	53.6	31	37	44
Operating cash flow	(3,094)	(3,112)	364	(4,537)	-	1,604	-	688	1,077	1,002
Tangible capital expenditure	(390)	(293)	(600)	(600)	0.0	(600)	0.0	(600)	(600)	(600)
Intangible capital expenditure	0	0	0	0	-	0	-	0	0	0
Net (acquisitions) / disposals	(660)	(834)	(303)	0	-	0	-	0	0	0
Other investing	44	332	0	0	-	0	-	0	0	0
Investing cash flow	(1,006)	(794)	(903)	(600)	33.6	(600)	0.0	(600)	(600)	(600)
Equity dividends paid	(523)	(703)	(1,043)	(1,374)	-31.7	(1,581)	-15.1	(1,877)	(2,228)	(2,638)
Share issues / (buybacks)	2,230	0	0	0	-	0	-	0	0	0
Other financing	(1,368)	820	0	0	-	0	-	0	0	0
Change in debt & pref shares	5,033	4,914	2,096	3,000	43.10	2,000	-33.33	2,000	0	0
Financing cash flow	5,373	5,032	1,053	1,626	54.4	419	-74.2	123	(2,228)	(2,638)
Cash flow inc/(dec) in cash	1,272	1,126	514	(3,511)	-	1,423	-	211	(1,751)	(2,236)
FX / non cash items	145	126	(1,188)	1,188	-	0	-	0	0	0
Balance sheet inc/(dec) in cash	1,417	1,251	(674)	(2,322)	-244.7	1,423	-	211	(1,751)	(2,236)

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

China State Construction International (3311.HK)

Valuation (x)	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
P/E (local GAAP, diluted)	13.9	17.0	14.6	9.3	8.1	6.6	5.7	4.9
P/E (UBS, diluted)	14.5	18.0	15.6	9.8	8.5	6.9	5.9	5.0
P/CEPS	12.6	15.9	13.3	8.7	7.6	6.2	5.4	4.6
Equity FCF (UBS) yield %	(11.9)	(7.4)	(0.5)	(12.4)	2.4	0.2	1.2	1.0
Net dividend yield (%)	2.0	1.8	2.0	3.2	3.7	4.4	5.2	6.2
P/BV x	2.3	2.9	2.5	1.9	1.6	1.3	1.2	1.0
EV/revenues (core)	1.0	1.4	1.1	0.5	0.5	0.4	0.3	0.2
EV/EBITDA (core)	11.4	16.4	10.9	4.8	4.1	3.2	2.5	1.8
EV/EBIT (core)	13.3	18.8	13.0	5.5	4.6	3.5	2.7	2.0
EV/OpFCF (core)	12.1	17.3	11.8	5.1	4.4	3.4	2.6	2.0
EV/op. invested capital	2.2	2.5	1.9	0.9	0.7	0.5	0.4	0.3
Enterprise value (HK\$m)	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
Market cap.	29,242	46,183	49,647	41,362	41,362	41,362	41,362	41,362
Net debt (cash)	(3,170)	(4,596)	(7,366)	(12,689)	(13,266)	(15,055)	(16,805)	(19,041)
Buy out of minorities	175	298	210	174	192	218	253	293
Pension provisions/other	0	0	0	0	0	0	0	0
Total enterprise value	26,247	41,885	42,491	28,848	28,289	26,526	24,810	22,615
Non core assets	(3,804)	(3,704)	(7,354)	(7,347)	(7,340)	(7,332)	(7,325)	(7,318)
Core enterprise value	22,443	38,181	35,137	21,501	20,949	19,194	17,485	15,297
Growth (%)	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
Revenue	32.0	23.1	25.6	20.8	13.0	18.2	17.4	16.9
EBITDA (UBS)	38.2	18.0	38.7	38.9	14.8	18.6	16.9	16.3
EBIT (UBS)	36.1	19.8	33.3	44.9	15.9	20.2	18.2	17.4
EPS (UBS, diluted)	27.9	22.0	23.9	32.6	15.8	23.4	15.7	19.0
Net DPS	23.1	31.3	23.8	31.7	15.1	18.8	18.7	18.4
Margins & Profitability (%)	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
Gross profit margin	11.3	11.5	11.2	12.8	13.0	13.1	13.1	13.1
EBITDA margin	9.1	8.7	9.6	11.1	11.2	11.3	11.2	11.2
EBIT margin	7.8	7.6	8.1	9.7	9.9	10.1	10.2	10.2
Net earnings (UBS) margin	9.5	9.8	9.7	10.8	11.0	11.2	11.4	11.6
ROIC (EBIT)	16.9	13.4	14.6	16.1	14.8	15.2	15.2	15.1
ROIC post tax	13.7	10.9	12.0	13.3	12.2	12.5	12.5	12.4
ROE (UBS)	17.8	17.7	18.1	20.3	20.3	20.9	21.4	21.8
Capital structure & Coverage (x)	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
Net debt / EBITDA	1.6	2.0	2.3	2.8	2.6	2.5	2.4	2.3
Net debt / total equity %	22.9	28.4	36.8	54.7	49.2	48.0	46.0	44.5
Net debt / (net debt + total equity) %	18.6	22.1	26.9	35.3	33.0	32.5	31.5	30.8
Net debt/EV %	14.1	12.0	21.0	59.0	63.3	78.4	96.1	NM
Capex / depreciation %	NM	NM	NM	NM	182.0	163.3	148.1	135.4
Capex / revenue %	1.8	1.1	1.8	1.5	1.3	1.1	0.9	0.8
EBIT / net interest	NM	NM	NM	NM	NM	NM	NM	NM
Dividend cover (UBS)	3.4	3.2	3.2	3.2	3.2	3.3	3.2	3.2
Div. payout ratio (UBS) %	29.1	31.3	31.3	31.5	31.3	30.1	30.9	30.8
Revenues by division (HK\$m)	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
Others	21,626	26,611	33,434	40,402	45,665	53,961	63,361	74,076
Total	21,626	26,611	33,434	40,402	45,665	53,961	63,361	74,076
EBIT (UBS) by division (HK\$m)	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
Others	1,694	2,029	2,705	3,920	4,542	5,459	6,453	7,573
Total	1,694	2,029	2,705	3,920	4,542	5,459	6,453	7,573

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

Forecast returns

Forecast price appreciation	+36.3%
Forecast dividend yield	3.4%
Forecast stock return	+39.7%
Market return assumption	9.3%
Forecast excess return	+30.4%

Statement of Risk

CSCI undertakes more and more BT/BOT projects, its capital requirements will increase. This would generate additional need for capital to support CSCI's new contract growth. The BT/BOT project contracts CSCI signs on the mainland require its own upfront capital. Local governments will repay CSCI only after these projects are completed and transferred to them. As such, the creditworthiness of local governments is critical. Meanwhile, the financial details of local government funding vehicles (LGFV) are generally not available, and this is an additional risk.

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UBS Investment Research: Global Equity Rating Definitions

12-Month Rating	Definition	Coverage ¹	IB Services ²
Buy	FSR is > 6% above the MRA.	47%	37%
Neutral	FSR is between -6% and 6% of the MRA.	42%	32%
Sell	FSR is > 6% below the MRA.	11%	21%
Short-Term Rating	Definition	Coverage ³	IB Services ⁴
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	less than 1%	less than 1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	less than 1%	less than 1%

Source: UBS. Rating allocations are as of 31 December 2014.

1:Percentage of companies under coverage globally within the 12-month rating category. 2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

3:Percentage of companies under coverage globally within the Short-Term rating category. 4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

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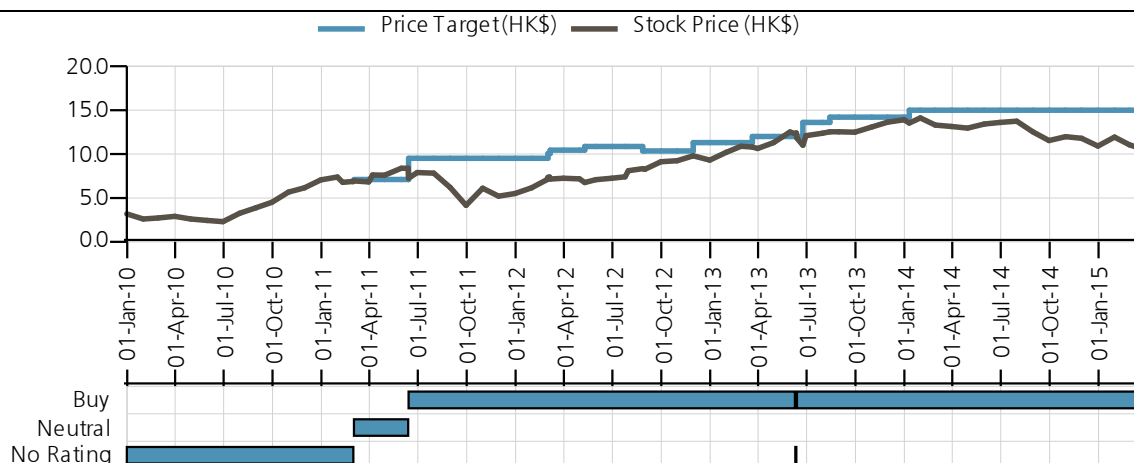
Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
China State Construction International	3311.HK		Buy	N/A HK\$10.64	20 Mar 2015

Source: UBS. All prices as of local market close.

Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

China State Construction International (HK\$)



Source: UBS; as of 20 Mar 2015

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