

Industrials
Electrical Equipment
 Equity – China

Overweight (V)

Target price (HKD)	53.20
Share price (HKD)	46.00
Potential return (%)	15.7

Note: Potential return equals the percentage difference between the current share price and the target price

Performance	1M	3M	12M
Absolute (%)	8.9	37.9	87.4
Relative ^A (%)	8.4	29.7	44.7

Index^A HSCEI

RIC 3898.HK
 Bloomberg 3898 HK

Market cap (USDm) 6,969
 Market cap (HKDm) 54,072

Enterprise value (CNYm) 38,640
 Free float (%) 42

Note: (V) = volatile (please see disclosure appendix)

21 March 2015

Anderson Chow*

Analyst
 The Hongkong and Shanghai Banking Corporation Limited
 +852 2996 6669
 andersonchow@hsbc.com.hk

Lesley Liu*

Analyst
 The Hongkong and Shanghai Banking Corporation Limited
 +852 2822 4524
 lesleyliu@hsbc.com.hk

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Zhuzhou CSR Times (3898 HK)

OW(V): First impression of 4Q14 results

- **FY14 NPAT increased 63% YoY to RMB2,395m in line with our forecast but 12% ahead of market expectation.**
- **Catalysts for the stock include progress of IGBT business and the timing of increase in sales to CNR Corp.**
- **Maintain OW(V), no change to earnings and TP HKD53.2**

Good set of results ahead of market expectation – The company's 4Q14 result appears to be better than market expectations according to Bloomberg consensus earnings but broadly in line with our forecast. FY14 NPAT increased 63% YoY to RMB2,395m. Operating cash flow in 2014 improved to RMB2,057m versus RMB726m in 2013. Balance sheet remains in a net cash position at end-2014. The 4Q14 result was not as strong as the previous quarters partly due to the commencement of rent payment (about RMB50m per quarter) for IGBT (insulated gate bipolar transistor) manufacturing facility to CSR Corp (1766 HK). In a business update provided by the management in February 2015, it noted the progress of the IGBT production facility is faster than expected and could lead to earlier breakeven than their initial projection. We currently expect the IGBT production facility to be breakeven at the bottom line in 2016.

The company management will host an analyst briefing at 4:30pm on 23 March at Hutchison House, Hong Kong. Key questions could include: 1. When could the IGBT production facility reach breakeven and the timing for acquiring the plant from CSR Corp. 2. Update on the timing and potential sales to CNR Corp (6199 HK) following the completion of CSR Corp and CNR Corp merger. 3. New order outlook for the company's national rail and subway electrical components. 4. The potential earnings impact from the company's development of a new generation of train operation safety equipment (i.e. this should be part of the rail signalling system on board the train) and 5. Any progress on its subway signalling system market development in China.

Beneficiary of Chinese rail equipment industry consolidation – We think Zhuzhou CSR may be a major beneficiary of the pending merger of CSR Corp and CNR Corp. Over time, we think Zhuzhou's domestic addressable market share would double as it substitutes the foreign component suppliers for CNR Corp's electric locomotive and MU (multiple units) product, as well as having the option to acquire the equivalent business from CNR Corp within five years of the merger completion. The stock is trading on 18x FY15e PER with 19% 3-year EPS CAGR, which looks reasonable on valuation basis.

Financials & valuation

Financial statements

Year to	12/2013a	12/2014e	12/2015e	12/2016e
Profit & loss summary (CNYm)				
Revenue	8,856	10,458	12,430	13,510
EBITDA	1,813	2,635	2,796	3,067
Depreciation & amortisation	-150	-166	-189	-212
Operating profit/EBIT	1,664	2,469	2,607	2,856
Net interest	27	73	73	74
PBT	1,704	2,682	2,820	3,056
HSBC PBT	1,704	2,682	2,820	3,056
Taxation	-237	-376	-423	-458
Net profit	1,467	2,308	2,398	2,599
HSBC net profit	1,467	2,308	2,398	2,599

Cash flow summary (CNYm)

Cash flow from operations	716	2,051	1,915	2,371
Capex	-290	-399	-460	-425
Cash flow from investment	-1,327	-399	-460	-425
Dividends	-411	-411	-692	-1,385
Change in net debt	-762	-1,252	-746	-518

Balance sheet summary (CNYm)

Intangible fixed assets	247	125	120	114
Tangible fixed assets	2,106	2,378	2,662	2,878
Current assets	10,813	10,968	12,807	13,934
Cash & others	3,136	4,387	5,133	5,652
Total assets	13,398	13,703	15,822	17,157
Operating liabilities	4,150	3,628	4,359	4,782
Gross debt	83	82	82	83
Net debt	-3,053	-4,305	-5,051	-5,569
Shareholders funds	9,427	9,843	11,231	12,156
Invested capital	5,880	5,456	6,098	6,492

Ratio, growth and per share analysis

Year to	12/2013a	12/2014e	12/2015e	12/2016e
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Y-o-y % change

Revenue	22.2	18.1	18.9	8.7
EBITDA	24.4	45.3	6.1	9.7
Operating profit	26.3	48.4	5.6	9.5
PBT	22.9	57.5	5.1	8.4
HSBC EPS	12.2	57.3	3.9	8.4

Ratios (%)

Revenue/IC (x)	1.8	1.8	2.2	2.1
ROIC	29.6	37.5	38.4	38.6
ROE	15.6	23.4	21.4	22.2
ROA	10.8	16.4	14.8	15.4
EBITDA margin	20.5	25.2	22.5	22.7
Operating profit margin	18.8	23.6	21.0	21.1
EBITDA/net interest (x)				
Net debt/equity	-31.9	-43.2	-44.4	-45.4
Net debt/EBITDA (x)	-1.7	-1.6	-1.8	-1.8

Per share data (CNY)

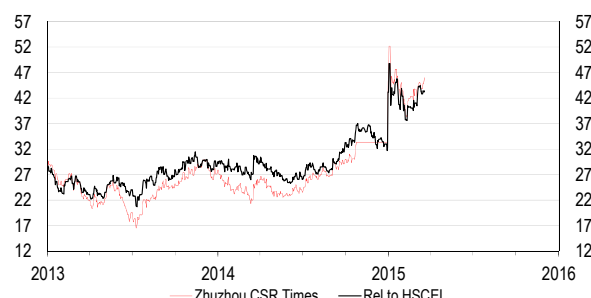
EPS reported (fully diluted)	1.25	1.96	2.04	2.21
HSBC EPS (fully diluted)	1.25	1.96	2.04	2.21
DPS	0.35	0.59	0.61	0.77
Book value	8.02	8.37	9.55	10.34

Valuation data

Year to	12/2013a	12/2014e	12/2015e	12/2016e
EV/sales	4.5	3.7	3.0	2.8
EV/EBITDA	22.0	14.7	13.6	12.2
EV/IC	6.8	7.1	6.2	5.8
PE*	29.4	18.7	18.0	16.6
P/Book value	4.6	4.4	3.8	3.6
Dividend yield (%)	1.0	1.6	1.7	2.1

Note: * = Based on HSBC EPS (fully diluted)

Price relative



Source: HSBC

Note: price at close of 19 Mar 2015

Zhuzhou CSR – FY14 result summary

RMBm	1Q14	2Q14	3Q14	4Q14	FY14A	FY13A	YoY%	HSBC FY14 Estimate	var %
Revenue	2,015	3,165	3,641	3,855	12,676	8,856	43.1%	10,458	21.2%
Cost of sales	(1,308)	(2,016)	(2,000)	(2,552)	(7,876)	(5,695)	38.3%	-6,316	24.7%
Gross profit	707	1,149	1,640	1,303	4,800	3,161	51.8%	4,142	15.9%
<i>GP margin</i>	35.1%	36.3%	45.1%	33.8%	37.9%	35.7%	6.1%	39.6%	
Other revenue and gains	-1	-87	60	217	190	81	134.8%	105	81.4%
Selling and distribution costs	-82	-192	-219	-387	-881	-498	76.7%	-554	58.9%
Administrative expenses	-255	-240	-378	-477	-1,349	-1,005	34.2%	-1,129	19.4%
Other operating expenses, net	-2	-28	-32	-38	-100	-75	32.6%	-94	6.0%
Profit/(loss) from operations [EBIT]	368	603	1,072	618	2,660	1,664	59.9%	2,469	7.7%
<i>EBIT margin</i>	18.2%	19.0%	29.4%	16.0%	21.0%	18.8%	11.7%	23.6%	
Finance costs	4	6	24	9	43	27	56.5%	73	-41.0%
Share of profit of an associate/jointly controlled entity	8	64	(20)	(0)	52	13	310.7%	140	-63.1%
Profit before tax	380	672	1,076	627	2,755	1,704	61.7%	2,682	
					0.0				
Income tax expenses	(65)	(132)	(184)	18	(363)	(237)	52.9%	-376	-3.4%
					0.0				
Profit for the year/period	315	540	893	644	2,392	1,466	63.1%	2,307	3.7%
<i>Net profit margin</i>	15.6%	17.1%	24.5%	16.7%	18.9%	16.6%		22.1%	
Attributable to:									
Equity holder of the Company	317	541	889	648	2,395	1,467	63.2%	2,308	3.8%
Minority interests	(2)	(1)	4	(4)	(3)	(1)	253.0%	(1)	124.4%
EPS (RMB)	0.27	0.46	0.76	0.55	2.04	1.33	53.4%	1.96	3.9%

Source: Company and HSBC

Valuation and risks

Zhuzhou CSR Times (3898 HK, OW(V), TP HKD53.2)

We value Zhuzhou using a DCF approach based on a WACC of 8.5%. Our key assumptions, which are all unchanged, include: risk-free rate of 3.5%; equity risk premium of 6.5%; terminal growth rate of 3.5%; and long-term target debt/(debt + equity) of 30% and an equity beta of 1. All assumptions remain unchanged.

Our DCF-based target price is HKD53.2 which implies a FY15e PE of 20.6x.

Key downside risks: the production yield of the new IGBT plant is insufficient; potential overseas acquisitions and expansion; potential business risks related to deep sea robotics business; and risk that the CSR Corp/CNR Corp merger does not proceed.

Disclosure appendix

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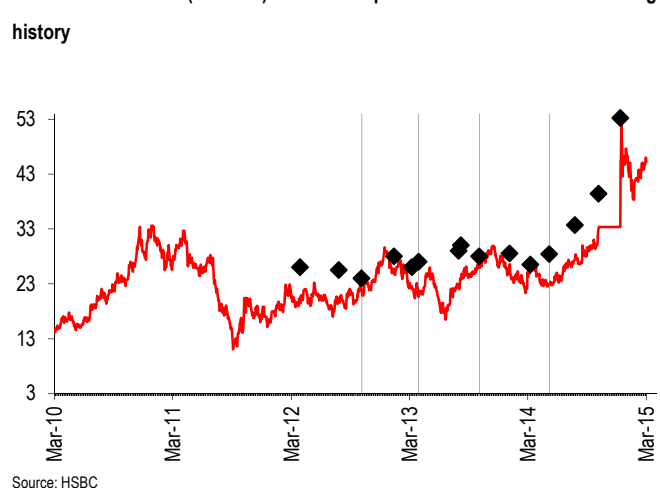
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Share price and rating changes for long-term investment opportunities

Zhuzhou CSR Times (3898.HK) Share Price performance HKD Vs HSBC rating history



Recommendation & price target history

From	To	Date
Overweight (V)	Neutral (V)	23 October 2012
Neutral (V)	Overweight (V)	17 April 2013
Overweight (V)	Neutral (V)	21 October 2013
Neutral (V)	Overweight (V)	25 May 2014
Target Price	Value	Date
Price 1	26.00	16 April 2012
Price 2	25.50	13 August 2012
Price 3	24.00	23 October 2012
Price 4	28.00	31 January 2013
Price 5	26.00	28 March 2013
Price 6	27.00	17 April 2013
Price 7	29.00	19 August 2013
Price 8	30.00	26 August 2013
Price 9	28.00	21 October 2013
Price 10	28.50	23 January 2014
Price 11	26.50	28 March 2014
Price 12	28.40	25 May 2014
Price 13	33.70	12 August 2014
Price 14	39.40	24 October 2014
Price 15	53.20	30 December 2014

Source: HSBC

HSBC & Analyst disclosures

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Company	Ticker	Recent price	Price Date	Disclosure
ZHUZHOU CSR TIMES	3898.HK	45.25	20-Mar-2015	4, 11

Source: HSBC

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Issuer of report

The Hongkong and Shanghai Banking Corporation Limited

Level 19, 1 Queen's Road Central
Hong Kong SAR

Telephone: +852 2843 9111

Fax: +852 2596 0200

Website: www.research.hsbc.com

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