

JPM-pp1

Asia Pacific Equity Research

22 March 2015

Zijin Mining Group - H (2899 HK)

Neutral

Price: HK\$2.19

20 Mar 2015

Price Target: HK\$2.20

PT End Date: 31 Dec 2015

First take FY14 results – In-line; FY15 output growth may not be enough to offset lower metal prices

Zijin's FY14 net profit of RMB2.35bn (+10% y/y) was in line with its preliminary results. While the company remains one of the few global mining companies to deliver earnings growth in a lower metal price environment, we see earnings headwinds from softer metal prices, with prices of gold and copper on average 3% and 16% below 2014's levels, respectively. While Zijin targets higher output in 2015 (mined gold +7%, copper +8% and zinc +118%), we believe it may not be enough to be offset lower metal prices. Our FY15 net profit forecast is 25% below the Street. Stay Neutral rated.

Result Highlights

- **FY14 results in-line.** Zijin's FY14 net profit of RMB2.35bn (+10% y/y) was in line with its preliminary results. Revenue was higher at RMB58.8bn (+18% y/y), thanks to higher sales volume of mined metals (gold +5%, copper +9%, zinc +28%) and refinery products (gold +62%, copper +12%, zinc +14%) offsetting lower metal prices. Gold, copper, zinc and iron ore accounted for 42%, 34%, 14% and 8% of FY14 gross profits, respectively.
- **Solid cost performance.** Unit costs of mined gold (-6% y/y) and mined zinc (-9% y/y) were lower, except for mined copper (+3% y/y). Of note was mined gold, which posted four consecutive quarterly unit cost declines (-7% q/q), reinforcing our view that cost issues associated with Zijinshan's mine depletion and degrading are now behind us. On the refinery side, gross margins of refinery gold and copper unexpectedly swung into negative territory (gold -0.2%; copper -1.3%) in 4Q, which we believe were due to hedging loss/inventory write-down and were the major culprits to lead to a 56% q/q decline in 4Q14 earnings.
- **Higher gearing levels, stable dividends.** Zijin's balance sheet weakened to some extent, with net gearing (ND/E) climbing higher to 54% (2013: 36%) on higher investing cash outflow, despite positive FCF (+RMB100m). ROE improved slightly to 7.0% (2013: 6.4%). Pleasingly, DPS was kept at 2013 levels of RMB0.08/share, highlighting Zijin's commitment to high dividend distribution to shareholders. The 2014 dividend payout was 70% (2013: 81%, 2012: 42%).
- **Guiding for higher output – gold +7%, copper +8% and zinc +118%.** For 2015, Zijin expects a sluggish global economy to keep metal prices at low levels, with more downside risk on copper due to a supply glut. It plans to increase mined gold output to 36t (+7% y/y), mined copper to 150kt (+8% y/y) and mined zinc to 210kt (+118 y/y). However, this may not be enough to offset lower metal prices ytd (gold -3%, copper -13% from 2014 average), in our view.

Stock Impact

- Given in-line FY14 results, we expected a muted market response to the results.

Investors and analysts briefing

Zijin will be hosting an investor presentation for its 2014 results.

Date: 23 March 2015 (Monday)

Time: 10:15 a.m. – 11:00 a.m.

Venue: Taishan Room, Level 5, Island Shangri-La Hotel, Pacific Place, Supreme Court Road, Central, HK

Medium: Mandarin

Table1: Zijin 's 2014 results (PRC GAAP)

(RMBm)	1Q13	2Q13	3Q13	4Q13	2013	1Q14	2Q14	3Q14	4Q14	2014	QoQ 4Q14	YoY 4Q14	YoY 2014
Operating income	11,772	14,216	11,041	12,743	49,772	10,762	13,224	16,615	18,160	58,761	9%	43%	18%
Operating costs	(9,538)	(11,971)	(8,883)	(10,454)	(40,846)	(9,267)	(10,835)	(14,139)	(16,641)	(50,882)	18%	59%	25%
Taxes	(95)	(163)	(158)	(303)	(719)	(161)	(216)	(242)	(219)	(838)	-10%	-28%	17%
Gross profit	2,138	2,082	2,000	1,986	8,206	1,334	2,173	2,234	1,300	7,040	-42%	-35%	-14%
Selling expenses	(87)	(176)	(129)	(134)	(526)	(97)	(213)	(310)	(286)	(906)	-8%	114%	72%
Admin expenses	(523)	(496)	(569)	(577)	(2,166)	(521)	(586)	(540)	(529)	(2,175)	-2%	-8%	0%
Impairment losses	0	(332)	178	(638)	(792)	(45)	(3)	(66)	(249)	(363)	274%	-61%	-54%
Changes in FV	25	(16)	(1)	11	19	107	(411)	392	(229)	(141)	nm	nm	nm
Investment income	33	(9)	(43)	(84)	(103)	150	150	7	444	751	6277%	nm	nm
Non-OP income	44	29	80	71	223	28	44	42	123	237	192%	73%	6%
Non-OP expenses	(67)	(37)	(82)	(224)	(410)	(52)	(72)	(58)	(191)	(373)	230%	-15%	-9%
Others	-	-	-	-	-	-	-	-	-	-	nm	nm	nm
EBIT	1,562	1,044	1,433	411	4,451	904	1,083	1,700	383	4,071	-77%	-7%	-9%
Financial expenses	(293)	(292)	(201)	53	(733)	(127)	(122)	(271)	(247)	(768)	-9%	nm	5%
Profits of assoc	12	50	25	29	117	46	66	(49)	(42)	21	-14%	nm	-82%

PBT	1,282	803	1,258	493	3,835	823	1,026	1,380	94	3,324	-93%	-81%	-13%
Income tax	(361)	(190)	(325)	(97)	(973)	(240)	(247)	(365)	163	(689)	nm	nm	-29%
MI	(201)	(234)	(241)	(60)	(736)	(63)	(191)	(156)	119	(290)	nm	nm	-61%
Net profit	720	379	691	336	2,125	521	589	860	376	2,345	-56%	12%	10%
EPS	0.03	0.02	0.03	0.02	0.10	0.02	0.03	0.04	0.02	0.11	-53%	6%	10%
Cash Flow													
Operating CF	710	1,327	3,281	3,525	8,842	605	1,159	1,070	3,486	6,321	226%	-1%	-29%
Investing CF	(1,384)	(2,105)	(2,985)	(2,005)	(8,480)	(1,886)	(2,470)	(1,411)	(3,485)	(9,252)	147%	74%	9%
Capex	(1,451)	(2,213)	(791)	(4,166)	(8,621)	(952)	(1,461)	(1,238)	(2,570)	(6,221)	108%	-38%	-28%
FCF	(740)	(886)	2,490	(642)	222	(347)	(303)	(168)	917	100	nm	nm	-55%
Margin													
Gross profit margin	18%	15%	18%	16%	16%	12%	16%	13%	7%	12%	-6pps	-8pps	-5pps
EBIT Margin	13%	7%	13%	3%	9%	8%	8%	10%	2%	7%	-8pps	-1pps	-2pps
Net income margin	6%	3%	6%	3%	4%	5%	4%	5%	2%	4%	-3pps	-1pps	0pps
Tax rate	28%	24%	26%	20%	25%	29%	24%	26%	-173%	21%	-199pps	-192pps	-5pps

Source: Company data, J.P. Morgan

Investment Thesis

Zijin is China's second-largest gold and copper miner. Within our gold coverage, the company is most vulnerable to the copper price shock, with gold and copper (from its mines and byproduct credits) accounting for 55% and 30% of its revenue. While we believe the company's effort over recent years to replenish gold assets and reduce costs will help Zijin to better weather the commodity storm, Zijin will be negatively affected should copper prices remain at current levels. Recent sell-down of A-shares by two major shareholders may also weigh on its share performance. Stay Neutral.

Valuation

Our Dec-15 price target for Zijin-H of HK\$2.20 equates to a 1.4x P/BV, 9.7x EV/EBITDA, and 4.4% dividend yield for an 8% ROE, based on our FY15 estimates. This is based on a blended average of P/BV-ROE valuation, EV/EBITDA multiple, P/E multiple, DCF-based NPV and EV/reserve method.

Risks to Rating and Price Target

- **Upside risk:** Stronger-than-expected gold prices, better-than-expected cost performance, faster-than-expected production growth, ongoing share buybacks, higher dividend distribution and M&As.
- **Downside risk:** Weaker-than-expected gold prices, higher-than-expected cost pressure, slower-than-expected production growth, worse-than-expected working capital control, higher-than-expected capex requirement.

Asia Metals and Mining

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Date	Rating	Share Price (HK\$)	Price Target (HK\$)
10-Mar-07	OW	4.12	6.04
11-Jul-07	OW	5.10	7.40
10-Sep-07	OW	8.84	10.80
29-Oct-07	OW	13.86	16.00
30-Jul-08	OW	6.26	9.20
19-Sep-08	N	3.90	5.80
25-Oct-08	N	1.42	3.83
22-Mar-11	N	6.07	--
03-Aug-14	OW	2.01	2.45
15-Jan-15	N	2.47	2.45
23-Jan-15	N	2.62	2.20

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