

China Coal Energy - H

FY2014 results - 2H14 losses to persist into first annual loss in FY15, cut PT to HKD3.60

China Coal Energy (CCE)'s disappointing finish to FY14 (4Q loss of Rmb546m) is set to continue, in our view. While the company targets FY15 revenue, coal output and unit coal cost to stay flat at 2014 levels, given the weak start to the year and management's poor guidance history, we believe this goal is unattainable. Near-term, we see CCE challenged by a heavy debt burden, lower than expected coal chemical profits and weak coal markets. We now expect CCE to swing to losses in FY15. Reiterate UW rating.

- 2014 result – big miss.** CCE's net income (IFRS) of RMB141m (-96% y/y) sharply missed Street expectations (JPMe RMB804m, Street RMB906m). Key earnings drags were 1) wider-than-expected 4Q loss of RMB546m, 2) higher finance cost (+210% y/y) and income tax (+89% y/y) wiping out savings from better unit cost (-7% y/y) and 3) RMB404m bad debts. Disappointingly, CCE recorded another year of negative FCF (RMB14.6Bn) which pushed net gearing (ND/E) higher to 74% (2013 57%). With a stretched balance sheet, CCE's decision to lift payout ratio to 40% (2013: 30%) appears unsustainable to us.
- 2015 targets unrealistic.** CCE provided a downbeat assessment of coal markets, noting that the domestic supply/demand imbalance will likely keep coal prices struggling at low levels. While CCE aims to maintain 2015 revenue (RMB70bn), coal output (c150Mt) and unit coal cost (below RMB195/t) broadly flat at 2014 levels, we view these targets unrealistic based on Jan output (-32% y/y) and CCE's poor guidance history.
- Stay UW – FY15 forecast to post first annual loss.** Given CCE's significant earnings miss, we sharply cut FY15/16 forecasts. We now expect it to swing to its first annual loss in FY15 (vs Street RMB801m profit) and scrap dividends, given QHD coal price ytd of RMB490/t (spot Rmb460/t), below 2014's average RMB518/t (Rmb4Q14 Rmb510/t). We expect CCE to retest historical lows and reduce our PT to HKD3.6/share.



Underweight

1898.HK, 1898 HK

Price: HK\$4.10

▼ **Price Target: HK\$3.60**
Previous: HK\$4.00

China

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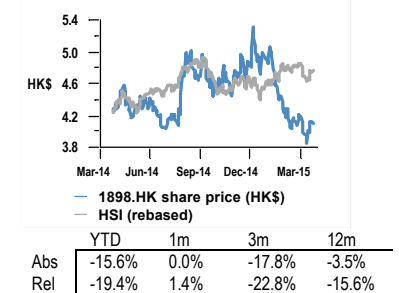
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Price Performance



China Coal Energy - H (Reuters: 1898.HK, Bloomberg: 1898 HK)

| Rmb in mn, year-end Dec | FY12A | FY13A | FY14A | FY15E | FY16E |
|-------------------------|---------|---------|---------|----------|----------|
| Revenue (Rmb mn) | 87,292 | 82,316 | 70,664 | 67,216 | 74,102 |
| Net Profit (Rmb mn) | 8,842 | 3,805 | 141 | (1,126) | 241 |
| EPS (Rmb) | 0.67 | 0.29 | 0.01 | (0.08) | 0.02 |
| DPS (Rmb) | 0.21 | 0.08 | 0.02 | 0.00 | 0.01 |
| Revenue growth (%) | (3.9%) | (5.7%) | (14.2%) | (4.9%) | 10.2% |
| EPS growth (%) | (11.2%) | (57.0%) | (96.3%) | (898.1%) | (121.4%) |
| ROCE | 7.8% | 3.4% | 1.1% | 0.2% | 1.0% |
| ROE | 10.4% | 4.4% | 0.2% | (1.3%) | 0.3% |
| P/E (x) | 4.9 | 11.4 | 308.7 | NM | 180.5 |
| P/BV (x) | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 |
| EV/EBITDA (x) | 5.2 | 9.7 | 17.4 | 16.5 | 12.5 |
| Dividend Yield | 6.4% | 2.5% | 0.7% | 0.0% | 0.2% |

Source: Company data, Bloomberg, J.P. Morgan estimates.

Company Data

| | |
|------------------------------|-----------|
| Shares O/S (mn) | 13,259 |
| Market Cap (Rmb mn) | 43,553 |
| Market Cap (\$ mn) | 7,008 |
| Price (HK\$) | 4.10 |
| Date Of Price | 23 Mar 15 |
| Free Float(%) | 43.4% |
| 3M - Avg daily vol (mn) | 20.52 |
| 3M - Avg daily val (HK\$ mn) | 90.20 |
| 3M - Avg daily val (\$ mn) | 11.6 |
| HSI | 2,4494.51 |
| Exchange Rate | 7.76 |
| Price Target End Date | 31-Dec-15 |

See page 11 for analyst certification and important disclosures, including non-US analyst disclosures.

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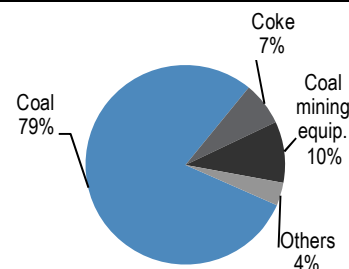
| Key catalysts for the stock price: | Upside risks to our view: | Downside risks to our view: |
|--|--|---|
| <ul style="list-style-type: none"> Coal price bottoming, summer restocking and production cuts from marginal players. (Positive) Deteriorating balance sheet (Negative). | <ul style="list-style-type: none"> Stronger-than-expected coal prices Lower-than-expected unit cost/capex Faster-than-expected additions in coal production | <ul style="list-style-type: none"> Weaker-than-expected coal prices Higher-than-expected cost pressure/capex Slower-than-expected additions in coal production |

| Key financial metrics | FY12A | FY13A | FY14E | FY15E | FY16E |
|-----------------------------|---------|---------|---------|---------|--------|
| Revenues (LC) | 87,292 | 82,316 | 70,664 | 67,216 | 74,102 |
| Revenue growth (%) | -3.9% | -5.7% | -14.2% | -4.9% | 10.2% |
| EBITDA (LC) | 17,504 | 12,085 | 7,807 | 8,828 | 11,778 |
| EBITDA margin (%) | 20.1% | 14.7% | 11.0% | 13.1% | 15.9% |
| Tax rate (%) | 25.1% | 27.8% | 28.2% | 28.2% | 28.2% |
| Net profit (LC) | 8,842 | 3,805 | 141 | -1,126 | 241 |
| EPS (LC) | 0.67 | 0.29 | 0.01 | -0.08 | 0.02 |
| EPS growth (%) | -11.2% | -57.0% | -96.3% | -898.1% | 121.4% |
| DPS (LC) | 0.21 | 0.08 | 0.02 | 0.00 | 0.01 |
| BVPS (LC) | 6.54 | 6.62 | 6.55 | 6.45 | 6.46 |
| Operating cash flow (LC mn) | 10,887 | 6,788 | 5,084 | 6,886 | 8,691 |
| Free cash flow (LC mn) | -16,165 | -17,995 | -13,210 | -6,720 | 372 |
| Interest cover (X) | 68.9 | 19.2 | 4.0 | 3.5 | 5.0 |
| Net margin (%) | 10.1% | 4.6% | 0.2% | -1.7% | 0.3% |
| Sales/assets (X) | 0.5 | 0.4 | 0.3 | 0.3 | 0.3 |
| Debt/equity (%) | 46.0% | 67.9% | 92.0% | 111.2% | 109.0% |
| Net debt/equity (%) | 32.9% | 57.0% | 74.4% | 85.2% | 86.4% |
| ROE (%) | 10.4% | 4.4% | 0.2% | -1.3% | 0.3% |

Valuation and price target basis

Our Dec-15 price target for China Coal-H is HKD3.60/share. This equates to 0.45x PB based on our FY15 estimates.

2015E Sales product mix



Key model assumptions

| December Y/E | FY13A | FY14A | FY15E | FY16E | FY17E |
|--|-------|-------|-------|-------|-------|
| Commercial coal output (Mt) | 119 | 114 | 106 | 116 | 125 |
| Total coal sales volumes (Mt) | 164 | 163 | 159 | 171 | 182 |
| Average ASP - Domestic Term Contract (RMB/tonne) | 425 | 368 | 357 | 357 | 376 |
| Average ASP - Domestic Spot Sales (RMB/tonne) | 373 | 287 | 272 | 280 | 299 |
| Newcastle Thermal Coal Prices (USD/tonne) | 84 | 70 | 59 | 61 | 67 |
| Qinhuangdao thermal coal prices (Rmb/tonne) | 588 | 518 | 500 | 515 | 550 |

Source: Bloomberg, Company and J.P. Morgan estimates.

Source: Bloomberg, Company and J.P. Morgan estimates.

Sensitivity analysis

| Sensitivity to | EBITDA | | EPS | |
|-------------------------------------|--------|-------|-------|-------|
| | FY15E | FY16E | FY15E | FY16E |
| 5% change in QHD thermal coal price | 14% | 12% | -61% | 324% |
| 5% change in coal sales volume | 19% | 16% | -79% | 422% |
| 5% change in coal unit cost | -19% | -15% | 79% | -405% |
| 1ppt change in finance cost | 0% | 0% | 50% | -253% |

Source: Bloomberg, Company and J.P. Morgan estimates.

JPM vs. consensus, change in estimates

| EPS | FY15E | FY16E |
|-----------|-------|-------|
| JPM old | 0.06 | 0.08 |
| JPM new | -0.08 | 0.02 |
| % chg | n.a. | -78% |
| Consensus | 0.06 | 0.10 |

Source: Bloomberg, Company and J.P. Morgan estimates.

Peer group valuation comparison table

| Company | Rating | FY End | Crncy | Price | Perf. YTD (%) | PE (x) | | PBV (x) | | EV/EBITDA (x) | | EBITDA Margin (%) | | ROE (%) | | Div Yield (%) | |
|---------------------|--------|--------|-------|-------|---------------|--------------|------------|------------|------------|---------------|------------|-------------------|-------------|------------|------------|---------------|------------|
| | | | | | | FY15E | FY16E | FY15E | FY16E | FY15E | FY16E | FY15E | FY16E | FY15E | FY16E | FY15E | FY16E |
| China Coal H | UW | Dec | HKD | 4.10 | -16% | 308.7 | -38.7 | 0.5 | 0.5 | 19.7 | 18.5 | 11.0 | 13.1 | 0.2 | -1.3 | 0.7 | 0.0 |
| China Coal A | UW | Dec | CNY | 6.97 | 1% | 655.0 | -82.1 | 1.1 | 1.1 | 19.7 | 18.5 | 11.0 | 13.1 | 0.2 | -1.3 | 0.3 | 0.0 |
| Shenhua H | N | Dec | HKD | 19.70 | -14% | 8.5 | 8.9 | 1.1 | 1.0 | 5.4 | 5.2 | 33.4 | 33.2 | 12.9 | 11.5 | 4.7 | 4.5 |
| Shenhua A | N | Dec | CNY | 19.99 | -1% | 10.8 | 11.3 | 1.3 | 1.3 | 5.4 | 5.2 | 33.4 | 33.2 | 12.9 | 11.5 | 3.7 | 3.5 |
| Yanzhou Coal H | N | Dec | HKD | 6.17 | -6% | 27.6 | 43.5 | 0.6 | 0.6 | 12.6 | 12.7 | 11.9 | 13.0 | 2.1 | 1.3 | 1.7 | 0.7 |
| Yanzhou Coal A | N | Dec | CNY | 14.49 | 10% | 80.9 | 127.6 | 1.7 | 1.7 | 12.6 | 12.7 | 11.9 | 13.0 | 2.1 | 1.3 | 0.6 | 0.2 |
| Weighted Avg | | | | | -2% | 104.6 | 8.5 | 1.3 | 1.2 | 8.3 | 8.0 | 27.9 | 28.1 | 9.9 | 8.5 | 3.0 | 2.8 |

Source: Company reports, Bloomberg, J.P. Morgan estimates. Closing prices as at 23 March 2015.

Key Issues

Key takeaways from result briefing - 2015 targets at risk

During the results briefing yesterday, the company reiterated its FY15 target for revenue, coal output and unit coal cost to stay at 2014 levels. We view these targets as unrealistic given weak market demand and management's poor guidance history. With a stretched balance sheet, CCE's decision to lift its payout ratio to 40% (2013: 30%) appears unsustainable to us. Other key takeaways from briefing: -

- Management acknowledged a 150Mt output is challenging but indicated that this output levels is necessary to absorb fixed costs. The company will aim to shift its production mix towards high-rank coal in a bid to cushion lower coal prices.
- CCE targets to keep "controlled cost" at 2014's level of RMB195/t, except for non-controlled costs such as railway costs. It noted that the new ad valorem resource tax (to replace local surcharges) have seen overall tax saving of RMB3/t.
- Investment return of coal chemical projects has slipped along with lower oil prices. Should oil price stay above USD40/lbb, management believed olefin projects can make RMB1,000-2,000/t profit based on spot ASP of RMB8,000-9,000/t (peak RMB: 11,000-12,000/t), and "a few hundred profit per tonne from fertilizers".
- Capex of RMB16.8Bn, 27% lower than 2014's RMB22.9Bn. It will be funded by bank borrowings and internal working capital. CCE targets to contain total debt/asset ratio below 60%. As the peak investment cycle during 12th FYP (2011-2015) comes to an end, capex is expected to fall beyond 2015, while the cash inflows from new projects should help bring down overall gearing.
- Inventory was built up in the past year but is expected to be cleared during Daqin Rail's overhaul (between April 6 to 30), for which CCE can step up sales efforts at the expense of small miners who are not able to get railway access.
- Relief policies to aid coal industry have not been successful in the context of sharper fall in demand ytd. However, management is hopeful that NDRC's increased efforts to clamp down on over-production, illegal mining, unsafe coal mines and production of low-rank coals should help address oversupply in medium term.

2014 result big miss - net income down 96% y/y

While CCE's net income under Chinese Accounting standards (CAS) of RMB754m (-79% y/y) fell within its guidance (75-85% decline) made in late-January (see [note](#)), NP under IFRS of RMB141m (-96% y/y) was significantly below expectations (JPMe RMB804m, Street RMB906m). The discrepancy arrived from RMB629m of profits associated with "special reserves and related deferred tax adjustment", which were not recognized in IFRS. Pleasingly, CCE increased its dividend payout ratio to 40% (vs 2013: 30%) of net income (CAS), leaving DPS of 25 cents RMB in line with consensus estimates.

Weak on all fronts.

The primary drivers of the weak results were lower coal sales (-3% y/y) and coal ASP (-12% y/y), leading to 15% decline in revenue. 4Q14 net loss (IFRS) of RMB546m (vs 3Q RMB93m loss) was wider than expected, despite higher coal prices (QHD +5% q/q) during the period. Key highlights included:

- a sharp increase in finance costs (+210% y/y) and higher tax expenses (+89% y/y), which wiped out savings from lower unit coal cost (-7% y/y) and SG&A (-6% y/y),
- negative FCF (-RMB14.6bn) continues to push net gearing (ND/E) higher to 74% (versus end-2013 57%),
- bad debts in accounts receivables of RMB403m (vs 2013: RMB70m) highlights risks to its trade receivables of RMB8.2bn, of which Rmb1.8bn are over 12 months.

Table 1: China Coal Energy – sales volume summary

| Sales Volume (mt) | 1Q13 | 2Q13 | 3Q13 | 4Q13 | 2013 | 1Q14 | 2Q14 | 3Q14 | 4Q14 | 2014 | QoQ% 4Q14 | YoY% 4Q14 | YoY% 2014 |
|---------------------|-------------|-------------|-------------|-------------|--------------|-------------|-------------|-------------|-------------|--------------|--------------|--------------|--------------|
| Thermal coal | 26.6 | 26.9 | 28.3 | 28.9 | 110.7 | 25.3 | 26.9 | 24.3 | 23.5 | 99.9 | -3% | -19% | -10% |
| Exports | 0.1 | 0.1 | 0.1 | 0.0 | 0.4 | 0.1 | 0.1 | 0.1 | 0.1 | 0.5 | -7% | nm | 21% |
| Domestic | 26.5 | 26.7 | 28.3 | 28.8 | 110.3 | 25.1 | 26.8 | 24.2 | 23.3 | 99.4 | -3% | -19% | -10% |
| - Contract | 15.1 | 18.2 | 18.6 | 17.3 | 69.1 | 20.8 | 22.1 | 20.1 | 19.5 | 82.5 | -3% | 13% | 19% |
| - Spot | 11.4 | 8.5 | 9.7 | 11.6 | 41.2 | 4.3 | 4.7 | 4.1 | 3.8 | 16.9 | -8% | -67% | -59% |
| Coking Coal | 1.2 | 1.6 | 0.9 | 0.9 | 4.6 | 1.5 | 1.7 | 1.4 | 1.6 | 6.2 | 13% | 89% | 35% |
| Total | 27.9 | 28.4 | 29.3 | 29.7 | 115.3 | 26.7 | 28.6 | 25.7 | 25.1 | 106.1 | -3% | -15% | -8% |

Source: Company reports and J.P. Morgan estimates.

Table 2: China Coal Energy – ASP summary (under CAS)

| Coal ASP | 1Q13 | 2Q13 | 3Q13 | 4Q13 | 2013 | 1Q14 | 2Q14 | 3Q14 | 4Q14 | 2014 | QoQ% 4Q14 | YoY% 4Q14 | YoY% 2014 |
|---------------------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|--------------|--------------|--------------|
| Self-Produced Coal | 448 | 424 | 401 | 418 | 422 | 401 | 364 | 338 | 364 | 367 | 8% | -13% | -13% |
| Thermal coal | 425 | 407 | 387 | 409 | 406 | 384 | 357 | 329 | 353 | 356 | 7% | -14% | -12% |
| Exports | 623 | 625 | 577 | n.a. | 596 | 575 | 554 | 543 | 509 | 545 | -6% | nm | -9% |
| Domestic | 424 | 406 | 386 | 409 | 406 | 383 | 356 | 328 | 352 | 355 | 7% | -14% | -13% |
| - Contract | 446 | 424 | 406 | 428 | 425 | 394 | 373 | 342 | 362 | 368 | 6% | -16% | -13% |
| - Spot | 394 | 368 | 343 | 381 | 373 | 330 | 278 | 265 | 273 | 287 | 3% | -28% | -23% |
| Coking Coal | 946 | 703 | 843 | 780 | 811 | 699 | 474 | 508 | 514 | 545 | 1% | -34% | -33% |
| Self produced ASP | 448 | 424 | 401 | 418 | 422 | 401 | 364 | 338 | 364 | 367 | 8% | -13% | -13% |
| Group ASP | 547 | 528 | 488 | 489 | 511 | 506 | 444 | 417 | 444 | 450 | 6% | -9% | -12% |

Source: Company reports and J.P. Morgan estimates.

Table 3: China Coal Energy – coal unit cost summary for self-produced coals (under CAS)

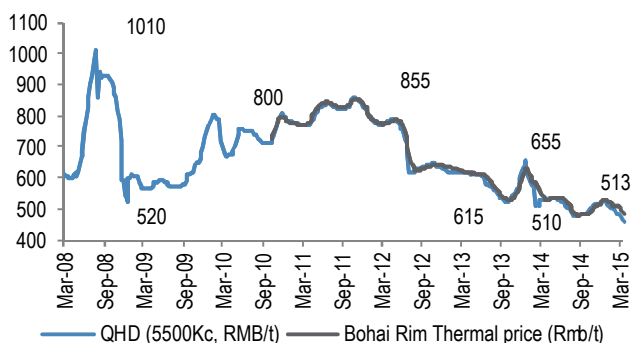
| Unit cost (RMB/t) | 1Q13 | 2Q13 | 3Q13 | 4Q13 | 2013 | 1Q14 | 2Q14 | 3Q14 | 4Q14 | 2014 | QoQ% 4Q14 | YoY% 4Q14 | YoY% 2014 |
|-----------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Costs under PRC GAAP | | | | | | | | | | | | | |
| Material costs | 72.8 | 50.2 | 61.5 | 76.9 | 65.8 | 63.4 | 48.2 | 54.4 | 72.5 | 59.5 | 33% | -6% | -10% |
| Labour costs | 27.2 | 33.8 | 27.5 | 29.0 | 29.4 | 28.2 | 31.9 | 25.9 | 35.9 | 30.7 | 39% | 24% | 4% |
| D&A | 30.7 | 47.3 | 27.6 | 27.3 | 32.9 | 32.9 | 43.7 | 24.4 | 45.2 | 36.9 | 85% | 66% | 12% |
| Repair costs | 6.7 | 11.7 | 10.6 | 10.2 | 9.9 | 8.7 | 6.8 | 5.5 | 8.8 | 7.4 | 59% | -14% | -25% |
| Others | 78.7 | 86.1 | 78.8 | 86.9 | 82.9 | 69.7 | 68.4 | 64.2 | 44.0 | 61.1 | -31% | -49% | -26% |
| Total unit cost | 216.2 | 229.1 | 205.9 | 230.3 | 220.8 | 202.9 | 199.0 | 174.3 | 206.5 | 195.6 | 18% | -10% | -11% |

Source: Company reports and J.P. Morgan estimates.

Earnings Revision

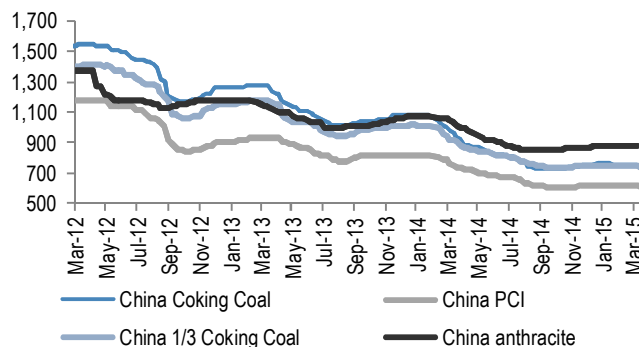
Given CCE's significant earnings miss, we sharply downgrade FY15/16 forecasts. We now expect the company to swing to its first ever annual loss in FY15 (Street RMB801m profit) with QHD coal price ytd of RMB490/t, below 2014's average RMB518/t.

Figure 1: China thermal coal prices (RMB/t) show bottoming



Source: Sxcoal, J.P. Morgan

Figure 2: China coking coal prices (RMB/t) stay weak



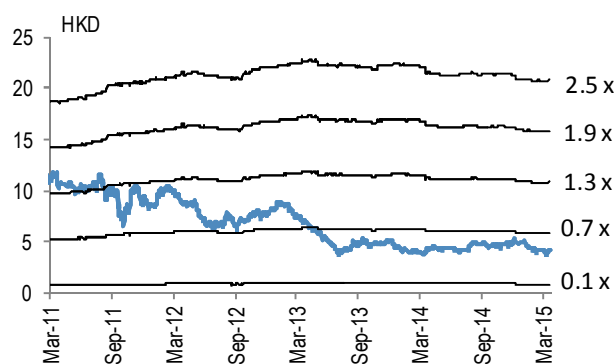
Source: Sxcoal, J.P. Morgan

Table 4: Earnings revision table

| China Coal (RMB mn) | Old | | | New | | | Change | | |
|---------------------|--------|--------|--------|---------|--------|--------|--------|-------|-------|
| | 2015E | 2016E | 2017E | 2015E | 2016E | 2017E | 2015E | 2016E | 2017E |
| Revenue | 69,505 | 73,626 | 84,471 | 67,216 | 74,102 | 82,928 | -3% | 1% | -2% |
| EBIT | 3,754 | 5,001 | 5,629 | 338 | 2,706 | 4,160 | -91% | -46% | -26% |
| NPAT | 760 | 1,089 | 1,862 | (1,126) | 241 | 1,018 | -248% | -78% | -45% |
| EPS | 0.06 | 0.08 | 0.14 | (0.08) | 0.02 | 0.08 | -248% | -78% | -45% |

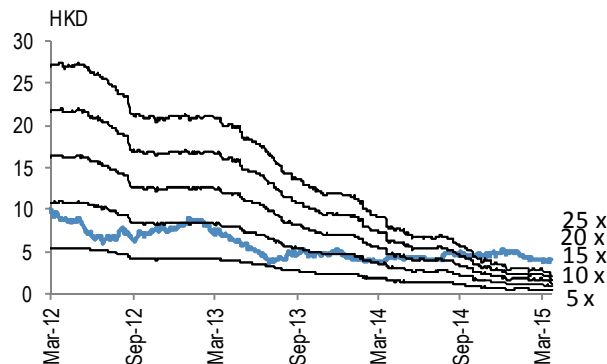
Source: Bloomberg, J.P. Morgan

Figure 3: China Coal H - 1 Yr Forward P/B Band Chart



Source: J.P. Morgan estimates, Bloomberg.

Figure 4: China Coal H - 1 Yr Forward P/E Band Chart



Source: J.P. Morgan estimates, Bloomberg.

2014 Result Summary

Table 5: China Coal Energy - 2014 Financial Results under IFRS

| (Rmb Mils) | 1H12 | 2H12 | 2012 | 1H13 | 2H13 | 2013 | 1H14 | 2H14 | 2014 | HoH% 2H14 | YoY% 2H14 | YoY% 2014 |
|--------------------------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|--------------|--------------|--------------|
| Revenue | 45,720 | 41,572 | 87,292 | 40,398 | 41,918 | 82,316 | 35,435 | 35,229 | 70,664 | -1% | -16% | -14% |
| Materials | -19,851 | -17,415 | -37,266 | -16,361 | -18,712 | -35,073 | -14,406 | -17,149 | -31,555 | -19% | 8% | 10% |
| Staff costs | -2,278 | -2,176 | -4,453 | -2,284 | -2,270 | -4,555 | -2,209 | -2,126 | -4,335 | 4% | 6% | 5% |
| Depreciation and amortization | -2,110 | -2,150 | -4,260 | -2,525 | -2,322 | -4,846 | -2,495 | -2,440 | -4,935 | 2% | -5% | -2% |
| Repairs and maintenance | -549 | -533 | -1,081 | -560 | -574 | -1,135 | -395 | -439 | -835 | -11% | 24% | 26% |
| Transportation cost | -5,459 | -5,987 | -11,446 | -5,910 | -7,106 | -13,016 | -6,277 | -5,557 | -11,834 | 11% | 22% | 9% |
| Sales taxes and surcharges | -722 | -649 | -1,372 | -654 | -640 | -1,294 | -622 | -456 | -1,078 | 27% | 29% | 17% |
| Others | -5,124 | -4,987 | -10,111 | -4,867 | -6,136 | -11,002 | -4,702 | -4,195 | -8,896 | 11% | 32% | 19% |
| Total cost of revenues | -36,093 | -33,896 | -69,989 | -33,161 | -37,760 | -70,920 | -31,106 | -32,362 | -63,468 | -4% | 14% | 11% |
| Gross Profit | 9,627 | 7,676 | 17,303 | 7,238 | 4,158 | 11,396 | 4,329 | 2,867 | 7,196 | -34% | -31% | -37% |
| less SG & A | -2,352 | -2,234 | -4,586 | -2,035 | -2,585 | -4,620 | -2,102 | -2,802 | -4,904 | -33% | -8% | -6% |
| add other income | 4 | -36 | -32 | 2 | -12 | -10 | 0 | 16 | 16 | nm | nm | nm |
| add other gains, net | 47 | 75 | 122 | 16 | 97 | 113 | 63 | 125 | 188 | 96% | 29% | 67% |
| Net operating profit | 7,327 | 5,480 | 12,807 | 5,221 | 1,658 | 6,879 | 2,291 | 206 | 2,497 | -91% | -88% | -64% |
| Net financing costs | -173 | -81 | -254 | -156 | -474 | -630 | -894 | -1,057 | -1,952 | -18% | -123% | -210% |
| Profits/(losses) of associates | 208 | 28 | 236 | 141 | 10 | 152 | 92 | 42 | 134 | -54% | 303% | -11% |
| Profit before tax | 7,362 | 5,427 | 12,789 | 5,206 | 1,195 | 6,401 | 1,488 | -809 | 679 | nm | nm | -89% |
| Tax | -1,837 | -1,377 | -3,214 | -1,307 | -474 | -1,781 | -431 | 239 | -192 | nm | nm | 89% |
| MI | -343 | -390 | -733 | -677 | -138 | -815 | -277 | -70 | -346 | 75% | 49% | 57% |
| Profit after tax | 5,182 | 3,660 | 8,842 | 3,221 | 584 | 3,805 | 780 | -639 | 141 | nm | nm | -96% |
| EPS (Rmb) | 0.39 | 0.28 | 0.67 | 0.24 | 0.04 | 0.29 | 0.06 | (0.05) | 0.01 | nm | nm | -96% |
| DPS (Rmb) | | | 0.210 | | | 0.081 | | | 0.024 | | | -70% |
| Ratio | | | | | | | | | | | | |
| Gross profit | 21.1% | 18.5% | 19.8% | 17.9% | 9.9% | 13.8% | 12.2% | 8.1% | 10.2% | -4.1pps | -1.8pps | -3.7pps |
| Net operating profit | 16.0% | 13.2% | 14.7% | 12.9% | 4.0% | 8.4% | 6.5% | 0.6% | 3.5% | -5.9pps | -3.4pps | -4.8pps |
| Profit before tax | 16.1% | 13.1% | 14.7% | 12.9% | 2.9% | 7.8% | 4.2% | -2.3% | 1.0% | -6.5pps | -5.1pps | -6.8pps |
| Profit after tax | 11.3% | 8.8% | 10.1% | 8.0% | 1.4% | 4.6% | 2.2% | -1.8% | 0.2% | -4.0pps | -3.2pps | -4.4pps |
| Tax rate | 25.0% | 25.4% | 25.1% | 25.1% | 39.6% | 27.8% | 29.0% | 29.6% | 28.2% | 0.6pps | -10pps | 0.4pps |
| Dividend payout | | | | | | 28.2% | | | 225.5% | | | |
| Cash flow analysis | | | | | | | | | | | | |
| Operating cash flow | 4,182 | 6,705 | 10,887 | 3,132 | 6,359 | 9,491 | 534 | 4,550 | 5,084 | 752% | -28% | -46% |
| Investing cash flow | -12,276 | -19,613 | -31,889 | -10,950 | -17,786 | -28,736 | -8,470 | -9,297 | -17,767 | -10% | 48% | 38% |
| Capex | -9,286 | -15,648 | -24,934 | -10,031 | -15,344 | -25,375 | -10,629 | -9,067 | -19,695 | 15% | 41% | 22% |
| FCF | -5,104 | -8,943 | -14,047 | -6,899 | -8,985 | -15,884 | -10,095 | -4,517 | -14,611 | 55% | 50% | 8% |
| Ratios | | | | | | | | | | | | |
| Net Debt/Equity | 19% | 33% | 33% | 43% | 57% | 57% | 67% | 74% | 74% | 7.7pps | 17.4pps | 17.4pps |
| Current Ratio | 1.9 | 1.4 | 1.4 | 1.3 | 1.1 | 1.1 | 1.1 | 1.1 | 1.1 | 3% | 4% | 4% |
| Quick Ratio | 1.6 | 1.3 | 1.3 | 1.1 | 0.9 | 0.9 | 0.9 | 1.0 | 1.0 | 3% | 2% | 2% |
| Inventory T/O Days | 39 | 36 | 35 | 40 | 33 | 35 | 51 | 49 | 50 | -5% | 48% | 42% |
| Accounts Receivable T/O Days | 42 | 50 | 48 | 61 | 56 | 57 | 75 | 70 | 70 | -7% | 24% | 22% |
| Accounts Payable T/O Days | 63 | 87 | 84 | 98 | 109 | 116 | 130 | 132 | 135 | 1% | 21% | 16% |
| Cash Conversion Cycle Days | 18 | -1 | -1 | 2 | -20 | -24 | -5 | -14 | -16 | -191% | 33% | 36% |
| ROA | 7% | 4% | 5% | 4% | 1% | 2% | 1% | -1% | 0% | -1.3pps | -1.2pps | -1.8pps |
| ROE | 13% | 9% | 10% | 8% | 1% | 4% | 2% | -1% | 0% | -3.3pps | -2.8pps | -4.2pps |

Source: Company reports and J.P. Morgan estimates.

Table 6: China Coal Energy – FY14 Financial Results under CAS

| | 1Q13 | 2Q13 | 3Q13 | 4Q13 | 2013 | 1Q14 | 2Q14 | 3Q14 | 4Q14 | 2014 | QoQ% 4Q14 | YoY% 4Q14 | YoY% 2014 |
|---------------------------------|--------------|--------------|------------|------------|--------------|------------|------------|------------|------------|--------------|--------------|--------------|--------------|
| Revenues | 20,125 | 20,273 | 19,211 | 22,707 | 82,316 | 16,859 | 18,576 | 16,645 | 18,585 | 70,664 | 12% | -18% | -14% |
| Cost of revenues | -12,997 | -13,931 | -13,147 | -16,067 | -56,142 | -10,945 | -12,946 | -12,224 | -13,320 | -49,434 | -9% | 17% | 12% |
| Business taxes and surcharge | -327 | -327 | -315 | -325 | -1,294 | -325 | -297 | -256 | -200 | -1,078 | 22% | 38% | 17% |
| Selling expenses | -3,146 | -3,101 | -3,720 | -3,820 | -13,788 | -3,211 | -3,396 | -2,852 | -3,095 | -12,554 | -8% | 19% | 9% |
| General & Admin exp | -1,032 | -951 | -1,164 | -1,273 | -4,420 | -1,068 | -917 | -965 | -1,229 | -4,179 | -27% | 3% | 5% |
| Net finance cost | -45 | -111 | -235 | -239 | -630 | -387 | -507 | -429 | -628 | -1,952 | -46% | -163% | -210% |
| Impairment loss on assets | -1 | -39 | 7 | -204 | -237 | 1 | -171 | 7 | -344 | -507 | nm | -69% | -114% |
| (L)/gain on changes in fair | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | nm | nm | nm |
| Investment income * | 25 | 62 | -9 | 8 | 85 | 18 | 55 | 88 | 295 | 457 | 235% | 3546% | 437% |
| Operating income | 2,602 | 1,874 | 628 | 788 | 5,891 | 942 | 398 | 13 | 64 | 1,416 | 380% | -92% | -76% |
| Non operating income | 13 | 31 | 33 | 96 | 172 | 16 | 67 | 35 | 182 | 300 | 421% | 91% | 74% |
| Non operating expenses* | -18 | -15 | -10 | 1 | -42 | -10 | -19 | -18 | -148 | -195 | -722% | nm | -366% |
| Profit before income tax | 2,596 | 1,891 | 650 | 884 | 6,022 | 948 | 446 | 30 | 98 | 1,521 | 223% | -89% | -75% |
| Income tax | -607 | -559 | -120 | -440 | -1,726 | -249 | -232 | 23 | 159 | -299 | 595% | nm | 83% |
| Minority interest | -334 | -245 | -90 | -50 | -720 | -161 | -65 | -80 | -149 | -455 | -86% | -196% | 37% |
| Profit for the period* | 1,655 | 1,086 | 440 | 394 | 3,576 | 538 | 148 | -27 | 107 | 767 | nm | -73% | -79% |
| IFRS | 1,853 | 1,369 | 479 | 105 | 3,805 | 614 | 166 | (93) | (546) | 141 | -484% | nm | -96% |

Source: Company reports and J.P. Morgan estimates.

Table 7: China Coal Energy – FY14 Operations Summary

| Year-end Dec (mn tons) | 1Q13 | 2Q13 | 3Q13 | 4Q13 | 2013 | 1Q14 | 2Q14 | 3Q14 | 4Q14 | 2014 | QoQ% 4Q14 | YoY% 4Q14 | YoY% 2014 |
|--------------------------------|-------|---------|-------|--------|--------|-------|---------|-------|--------|--------|--------------|--------------|--------------|
| Commercial coal output | 29.66 | 29.18 | 29.83 | 30 | 118.68 | 29.99 | 30.49 | 28.69 | 25 | 114.40 | -12% | -16% | -4% |
| Coal sales volume | 36.78 | 38.39 | 39.38 | 46 | 161.01 | 33.32 | 41.80 | 39.90 | 42 | 156.89 | 5% | -10% | -3% |
| - Self-produced coal | 27.85 | 28.44 | 29.25 | 30 | 115.31 | 26.70 | 28.56 | 25.75 | 25 | 106.09 | -3% | -16% | -8% |
| <u>Thermal coal</u> | 26.61 | 26.86 | 28.34 | 29 | 110.73 | 25.25 | 26.87 | 24.32 | 23 | 99.91 | -3% | -19% | -10% |
| Export | 0.12 | 0.14 | 0.08 | 0 | 0.43 | 0.13 | 0.12 | 0.14 | 0 | 0.52 | -7% | 44% | 21% |
| Term contract | 0.00 | 0.26 | 0.08 | 0 | 0.43 | 0.00 | 0.25 | 0.14 | 0 | 0.52 | -7% | 44% | 21% |
| Spot sales | 0.12 | -0.12 | 0.00 | 0 | 0.00 | 0.13 | -0.13 | 0.00 | 0 | 0.00 | nm | nm | nm |
| Domestic sales | 26.49 | 26.72 | 28.26 | 29 | 110.30 | 25.12 | 26.75 | 24.18 | 23 | 99.39 | -3% | -19% | -10% |
| Term contract | 15.09 | 18.18 | 18.58 | 17 | 69.11 | 20.79 | 22.09 | 20.05 | 20 | 82.47 | -3% | 13% | 19% |
| Spot sales | 11.40 | 8.54 | 9.68 | 12 | 41.19 | 4.33 | 4.66 | 4.12 | 4 | 16.92 | -8% | -67% | -59% |
| <u>Coking coal</u> | 1.24 | 1.58 | 0.91 | 1 | 4.58 | 1.45 | 1.69 | 1.43 | 2 | 6.18 | 13% | 89% | 35% |
| Export | 0.00 | 0.00 | 0.00 | 0 | 0.00 | 0.00 | 0.00 | 0.00 | 0 | 0.00 | nm | nm | nm |
| Domestic sales | 1.24 | 1.58 | 0.91 | 1 | 4.58 | 1.45 | 1.69 | 1.43 | 2 | 6.18 | 13% | 89% | 35% |
| Term contract | 0.00 | 0.00 | 0.00 | 0 | 0.00 | 0.00 | 0.00 | 0.00 | 0 | 0.00 | nm | nm | nm |
| Spot sales | 1.24 | 1.58 | 0.91 | 1 | 4.58 | 1.45 | 1.69 | 1.43 | 2 | 6.18 | 13% | 89% | 35% |
| - Coal trading | 7.97 | 9.12 | 9.38 | 15 | 41.19 | 5.71 | 12.19 | 12.32 | 16 | 46.34 | 31% | 10% | 13% |
| - Import/export service | 0.96 | 0.83 | 0.75 | 2 | 4.51 | 0.91 | 1.05 | 1.83 | 1 | 4.46 | -63% | -66% | -1% |
| Coke production output | 0.46 | 0.46 | 0.49 | 0 | 1.91 | 0.48 | 0.48 | 0.50 | 0 | 1.94 | -1% | -1% | 2% |
| Equipment (Rmb mn) | 1,482 | 1,847.9 | 1,664 | 59,806 | 64,800 | 1,483 | 1,737.3 | 1,180 | 51,200 | 55,600 | 4239% | -14% | -14% |

Source: Company reports and J.P. Morgan estimates.

Investment Thesis, Valuation and Risks

China Coal Energy - H (*Underweight; Price Target: HK\$3.60*)

Investment Thesis

China Coal Energy (CCE) is the second-largest coal miner in China behind China Shenhua with an annual coal production capacity of c120Mt. It reported disappointing FY14 results. With coal markets still heavily oversupplied, CCE's heavy capex plans, negative free cash generation, diminishing returns from coal chemical investment and aging trade receivables remains a concern. Stay UW, with a PT of HK\$3.60.

Valuation

Our Dec-15 price target for China Coal-H is HK\$3.60/share. This equates to 0.45x P/B based on our FY15 estimates. The P/B of 0.45x is based on our forecast of sustainable ROE of c4%, derived from our near-term forecast ROE (c0% in 2015) and 1% between 2016 and 2017.

Risks to Rating and Price Target

Upside risks

- Stronger-than-expected coal prices
- Lower-than-expected unit cost/capex
- Faster-than-expected additions in coal production

Downside risks

- Weaker-than-expected coal prices
- Higher-than-expected cost pressure/capex
- Slower-than-expected additions in coal production

China Coal Energy - H: Summary of Financials

| Income Statement | | | | | | Cash flow statement | | | | | |
|-------------------------------|---------|---------|----------|----------|---------|-------------------------------|----------|----------|----------|----------|----------|
| Rmb in millions, year end Dec | FY13 | FY14 | FY15E | FY16E | FY17E | Rmb in millions, year end Dec | FY13 | FY14 | FY15E | FY16E | FY17E |
| Revenues | 82,316 | 70,664 | 67,216 | 74,102 | 82,928 | EBIT | 6,879 | 2,497 | 338 | 2,706 | 4,160 |
| % change Y/Y | (5.7%) | (14.2%) | (4.9%) | 10.2% | 11.9% | Depr. & amortization | 5,206 | 5,310 | 8,491 | 9,072 | 9,154 |
| Gross Margin | 13.8% | 10.2% | 7.2% | 8.4% | 9.7% | Change in working capital | (534) | 322 | (103) | 175 | 175 |
| EBITDA | 12,085 | 7,807 | 8,828 | 11,778 | 13,314 | Taxes | (2,856) | (192) | 591 | (127) | (534) |
| % change Y/Y | (31.0%) | (35.4%) | 13.1% | 33.4% | 13.0% | Other | (1,689) | (689) | (375) | (798) | 339 |
| EBITDA margin | 14.7% | 11.0% | 13.1% | 15.9% | 16.1% | Cash flow from operations | 6,788 | 5,084 | 6,886 | 8,691 | 10,687 |
| EBIT | 6,879 | 2,497 | 338 | 2,706 | 4,160 | Capex | (25,237) | (19,695) | (16,830) | (10,000) | (10,000) |
| % change Y/Y | (46.3%) | (63.7%) | (86.5%) | 700.9% | 53.7% | Disposal/(purchase) | 137 | 0 | 0 | 0 | 0 |
| EBIT Margin | 8.4% | 3.5% | 0.5% | 3.7% | 5.0% | Net Interest | (630) | (1,952) | (2,514) | (2,342) | (2,352) |
| Net Interest | (630) | (1,952) | (2,514) | (2,342) | (2,352) | Free cash flow | (17,995) | (13,210) | (6,720) | 372 | 2,375 |
| Earnings before tax | 6,401 | 679 | (2,092) | 448 | 1,892 | Equity raised/(repaid) | - | - | - | - | - |
| % change Y/Y | (49.9%) | (89.4%) | (408.0%) | (121.4%) | 322.1% | Debt raised/(repaid) | 14,827 | 24,745 | 18,129 | (2,000) | (3,000) |
| Tax | (1,781) | (192) | 591 | (127) | (534) | Other | 8,431 | (4,086) | 375 | (80) | (339) |
| as % of EBT | 27.8% | 28.2% | (28.2%) | 28.2% | 28.2% | Dividends paid | (2,784) | (1,074) | (320) | 0 | (72) |
| Net income (reported) | 3,805 | 141 | (1,126) | 241 | 1,018 | Beginning cash | 13,223 | 11,233 | 18,132 | 26,372 | 22,983 |
| % change Y/Y | (57.0%) | (96.3%) | (898.1%) | (121.4%) | 322.1% | Ending cash | 11,233 | 18,132 | 26,372 | 22,983 | 20,258 |
| Shares outstanding | 13,259 | 13,259 | 13,259 | 13,259 | 13,259 | DPS | 0.08 | 0.02 | 0.00 | 0.01 | 0.02 |
| EPS (reported) | 0.29 | 0.01 | (0.08) | 0.02 | 0.08 | | | | | | |
| % change Y/Y | (57.0%) | (96.3%) | (898.1%) | (121.4%) | 322.1% | | | | | | |
| Balance sheet | | | | | | Ratio Analysis | | | | | |
| Rmb in millions, year end Dec | FY13 | FY14 | FY15E | FY16E | FY17E | Rmb in millions, year end Dec | FY13 | FY14 | FY15E | FY16E | FY17E |
| Cash and cash equivalents | 11,233 | 18,132 | 26,372 | 22,983 | 20,258 | Net profit margin | 4.6% | 0.2% | (1.7%) | 0.3% | 1.2% |
| Accounts receivable | 12,895 | 13,459 | 12,803 | 14,114 | 15,796 | SG&A/Sales | 5.6% | 6.9% | 6.9% | 5.0% | 5.0% |
| Inventories | 6,806 | 8,622 | 9,132 | 10,067 | 11,266 | Interest coverage (x) | 19.2 | 4.0 | 3.5 | 5.0 | 5.7 |
| Others | 16,793 | 15,567 | 23,534 | 24,237 | 25,138 | Net debt to equity | 57.0% | 74.4% | 85.2% | 86.4% | 85.3% |
| Current assets | 47,728 | 55,781 | 71,840 | 71,401 | 72,458 | Sales/assets | 0.4 | 0.3 | 0.3 | 0.3 | 0.3 |
| LT investments | 10,086 | 10,806 | 10,806 | 10,806 | 10,806 | Assets/equity | 2.3 | 2.6 | 2.9 | 3.0 | 3.0 |
| Net fixed assets | 110,060 | 126,418 | 129,555 | 130,850 | 132,058 | ROE | 4.4% | 0.2% | (1.3%) | 0.3% | 1.2% |
| Total Assets | 216,520 | 244,012 | 260,093 | 260,582 | 262,484 | ROA | 1.9% | 0.1% | (0.4%) | 0.1% | 0.4% |
| Liabilities | | | | | | ROCE | 3.4% | 1.1% | 0.2% | 1.0% | 1.5% |
| Short-term loans | 10,320 | 12,837 | 12,837 | 12,837 | 12,837 | | | | | | |
| Payables | 22,631 | 23,421 | 23,030 | 25,059 | 27,626 | | | | | | |
| Others | 10,547 | 12,671 | 12,459 | 13,557 | 14,946 | | | | | | |
| Total current liabilities | 43,498 | 48,929 | 48,326 | 51,452 | 55,408 | | | | | | |
| Long-term debt | 59,643 | 81,871 | 100,000 | 98,000 | 95,000 | | | | | | |
| Other liabilities | 10,286 | 10,283 | 10,283 | 9,405 | 9,405 | | | | | | |
| Total Liabilities | 113,427 | 141,083 | 158,609 | 158,857 | 159,814 | | | | | | |
| Shareholder's equity | 87,811 | 86,904 | 85,458 | 85,699 | 86,645 | | | | | | |
| BVPS | 6.62 | 6.55 | 6.45 | 6.46 | 6.53 | | | | | | |

Source: Company reports and J.P. Morgan estimates.

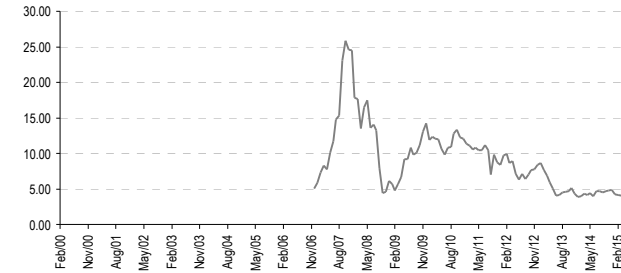
JPM Q-Profile
China Coal Energy Co. Ltd. Class H (CHINA / Energy)

As Of: 23-Mar-2015

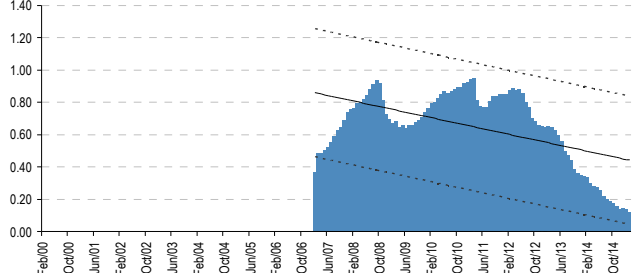
Global Equity Quantitative Analysis

Quant_Strategy@jpmorgan.com

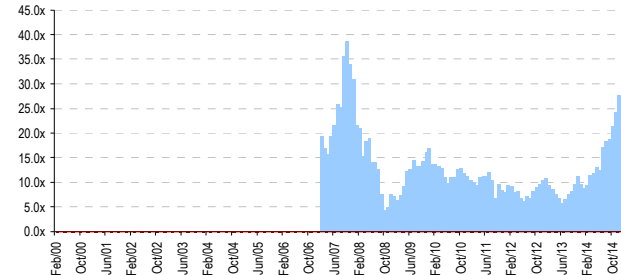
Local Share Price **Current: 4.11**



12 Mth Forward EPS **Current: 0.12**



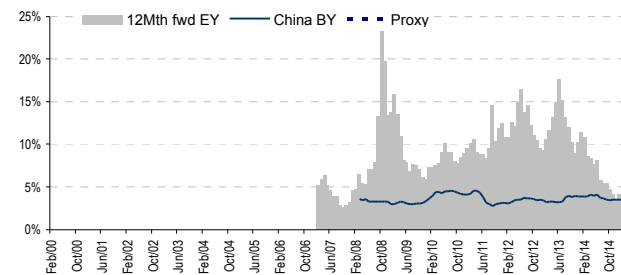
PE (1Yr Forward) **Current: 27.1x**



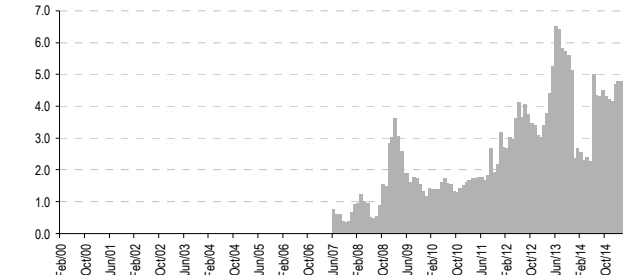
P/E Relative to China Index **Current: 2.80**



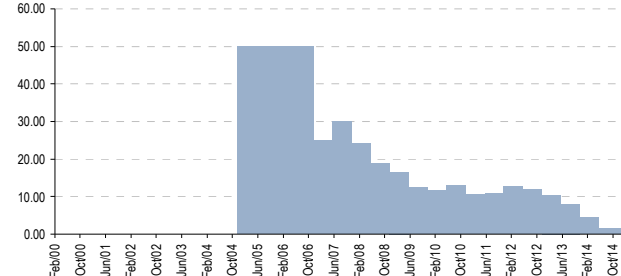
Earnings Yield (& Local Bond Yield) **Current: 4%**



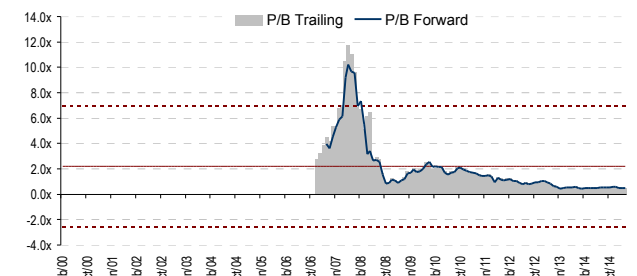
Dividend Yield (Trailing) **Current: 4.79**



ROE (Trailing) **Current: 1.56**



Price/Book (Value) **Current: 0.5x**



Summary

| | | | | | | | | | | | |
|---|---------------|-----------------------|------------|--------------------------|----------------|----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| China Coal Energy Co. Ltd. Class H | | TICKER 1898 HK | | As Of: 23-Mar-15 | | | | | | | |
| CHINA | | | | Local Price: 4.11 | | | | | | | |
| Energy | | | | EPS: 0.12 | | | | | | | |
| | Latest | Min | Max | Median | Average | 2 S.D.+ | 2 S.D. - | % to Min | % to Max | % to Med | % to Avg |
| 12mth Forward PE | 27.07x | | | | | | | | | | |
| P/BV (Trailing) | 0.50 | 0.46 | 11.76 | 1.42 | 2.21 | 6.99 | -2.56 | -8% | 2265% | 186% | 346% |
| Dividend Yield (Trailing) | 4.79x | 0.00 | 6.54 | 1.86 | 2.40 | 5.61 | -0.81 | -100% | 36% | -61% | -50% |
| ROE (Trailing) | 1.56 | 1.56 | 50.00 | 12.72 | 20.45 | 52.52 | -11.62 | 0% | 3102% | 714% | 1209% |

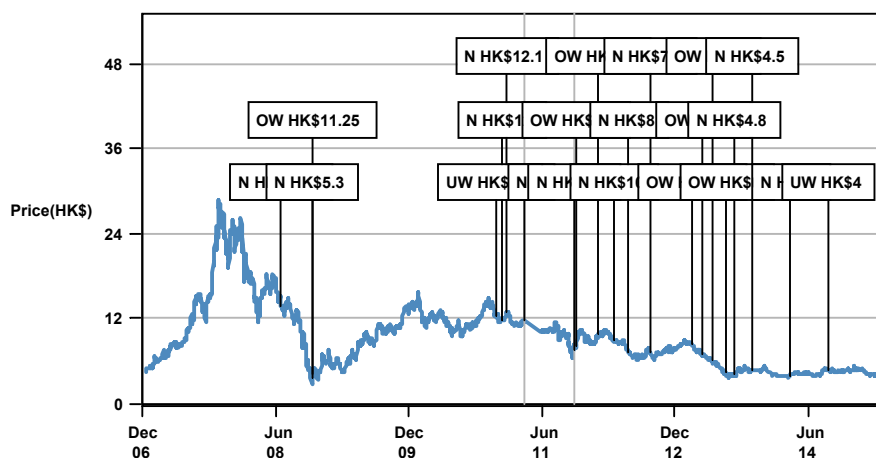
Source: Bloomberg, Reuters Global Fundamentals, IBES CONSENSUS, JPMorgan Quantitative & Derivative Strategy

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China Coal Energy - H (1898.HK, 1898 HK) Price Chart



Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.
 Break in coverage Mar 22, 2011 - Oct 08, 2011.

| Date | Rating | Share Price (HK\$) | Price Target (HK\$) |
|-----------|--------|--------------------|---------------------|
| 24-Jun-08 | N | 13.70 | 15.70 |
| 27-Oct-08 | N | 3.62 | 5.30 |
| 31-Oct-08 | OW | 4.20 | 11.25 |
| 25-Nov-10 | UW | 12.48 | 11.50 |
| 16-Dec-10 | N | 11.76 | 12.00 |
| 06-Jan-11 | N | 12.96 | 12.10 |
| 22-Mar-11 | N | 11.82 | -- |
| 08-Oct-11 | N | 7.51 | 8.50 |
| 23-Oct-11 | OW | 8.13 | 9.50 |
| 20-Jan-12 | OW | 9.85 | 11.00 |
| 28-Mar-12 | N | 8.89 | 10.00 |
| 20-May-12 | N | 7.39 | 8.00 |
| 20-Aug-12 | N | 7.31 | 7.50 |
| 07-Feb-13 | OW | 8.40 | 9.50 |
| 17-Mar-13 | OW | 6.97 | 9.00 |
| 28-Apr-13 | OW | 6.30 | 8.00 |
| 26-Jun-13 | OW | 4.38 | 6.00 |
| 02-Aug-13 | N | 4.16 | 4.80 |
| 14-Oct-13 | N | 4.75 | 4.50 |
| 19-Mar-14 | N | 3.96 | 4.00 |
| 19-Aug-14 | UW | 4.82 | 4.00 |

The chart(s) show J.P. Morgan's continuing coverage of the stocks; the current analysts may or may not have covered it over the entire period.

J.P. Morgan ratings or designations: OW = Overweight, N= Neutral, UW = Underweight, NR = Not Rated

Explanation of Equity Research Ratings, Designations and Analyst(s) Coverage Universe:

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