

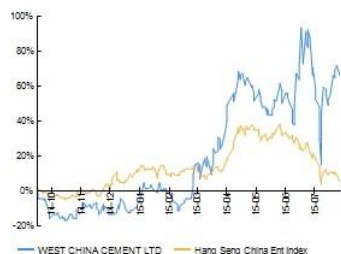
17 January, 2017

BUY
Unchanged

Market Data: 16 Jan

| | |
|--------------------------|-----------|
| Closing Price (HK\$) | 0.95 |
| Price Target (HK\$) | 1.2 |
| HSCCI | 9665 |
| HSCCI | 3700 |
| 52-week High/Low (HK\$) | 1.16/0.70 |
| Market Cap (US\$m) | 664 |
| Market Cap (HK\$m) | 5150 |
| Shares Outstanding (m) | 4,517 |
| Exchange Rate (Rmb-HK\$) | 1.26 |

Price Performance Chart:



Source: Bloomberg

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Related Reports

"West China Cement (2233 HK) - Building roads" 19 October 2016

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扭亏为盈

西部水泥 (2233:HK)

Financial summary and valuation

| | 2014 | 2015 | 2016E | 2017E | 2018E |
|--------------------|--------|---------|---------|-------|-------|
| Revenue (Rmbm) | 3,883 | 3,501 | 4,631 | 5,009 | 5,152 |
| YoY (%) | (6.8) | (9.8) | 32.3 | 8.2 | 2.9 |
| Net income (Rmbm) | 36 | (309) | 143 | 368 | 425 |
| YoY (%) | (90.5) | (961.2) | (146.1) | 158.2 | 15.4 |
| EPS (Rmb) | 0.01 | (0.06) | 0.03 | 0.07 | 0.08 |
| Diluted EPS (Rmb) | 0.01 | (0.06) | 0.03 | 0.07 | 0.08 |
| ROE (%) | 0.7 | (5.2) | 4.3 | 10.1 | 11.5 |
| Debt/asset (%) | 0.08 | 0.05 | 0.05 | 0.05 | 0.04 |
| Dividend yield (%) | 0.21 | (1.66) | 0.70 | 1.82 | 2.10 |
| PE (x) | 95.7 | (12.2) | 28.8 | 11.2 | 9.7 |
| PB (x) | 0.7 | 0.6 | 0.7 | 0.7 | 0.6 |
| EV/Ebitda (x) | 6.3 | 10.4 | 4.8 | 3.0 | 2.3 |

Note: Diluted EPS is calculated as if all outstanding convertible securities, such as convertible preferred shares, convertible debentures, stock options and warrants, were exercised.

股票优异表现 在我们 2016 年 10 月 18 日给予西部水泥买入评级之后，西部水泥股价涨幅 21.8%，超涨恒生国企指数 17.94%。由于对 2H16 毛利的乐观态度，我们上调西部水泥 16 年 EPS 从 0.004 人民币上调至 0.026 元（由亏转盈），2017 年 EPS 从人民币 0.05 元上调至 0.068 元（同比增长 162%），18 年的 EPS 从人民币 0.06 元上调至 0.078 元（同比增长 15%），我们维持目标价 1.20 港币和买入评级不变。

2H16 毛利复苏 由于陕西水泥价格自 2016 年的 7 月以来上涨了每吨 100 元，我们预期西部水泥 2H16 的吨价格为人民币 305 元，环比上涨 103 元，同比上涨了 100 元。尽管煤价和其他成本在下半年涨幅较大，西部水泥和海螺在运营上合作，尤其是成本消减方面让我们对其毛利乐观。西部水泥的吨成本预计在人民币 255 元，比上半年上涨了约 79 元，同比增加 78 元。因此，我们预计 16 年下半年吨毛利为 50 元，对比 16 年上半年的 18 元和 15 年下半年的 28 元。今年下半年的强劲的毛利复苏使得全年毛利在每吨 38 元左右。

17 年稳定的基建需求。 陕西省的水泥需求大部分取决于基建项目，尤其是轨道和道路交通。但是，由于资金不到位，15 年下半年以来当地基建速度放缓且水泥价格低迷。最近，由于基建需求抬头，特别是轨道和高速公路工程的加速，水泥价格稳步回升。西安的高铁项目将会是该区域未来三年基建的强劲支撑。我们预计西部水泥将是当地基建项目的最大收益房。公司已经签约了 10 个高速公路项目和 9 个铁路项目。

潜在并购的催化剂。 海螺和西部水泥方面对潜在的并购保持乐观，但是大家对于相应的时间线依然不确定。根据海螺管理层，双方目前在成本缩减，效率提高等运营方面进行深度合作。我们预计双方的并购将会在今年重新开放，目前离 12 个月的限制期已经只剩下不到 5 个月的时间。海螺目前占有西部水泥股份的 21.5%且成本在 1.59 元港币。

维持买入 我们看好陕西水泥市场的结构变化和西部水泥在当地的盈利能力的提升。但是，由于对 2H16 毛利的乐观态度，我们上调西部水泥 16 年 EPS 从 0.004 人民币上调至 0.026 元（由亏转盈），2017 年 EPS 从人民币 0.05 元上调至 0.068 元（同比增长 162%），18 年的 EPS 从人民币 0.06 元上调至 0.078 元（同比增长 15%），我们维持目标价 1.20 港币，对应 16 年的吨企业价值为人民币 290 元。由于 26% 的上下空间，我们维持买入评级。

West China Cement (WCC) stock price has increased c.21.8% since end-October, outperforming the Hong Kong Stock Exchange Hang Seng China Enterprises Index (HSCEI:IND) by c.18%. Given our expectation for higher margins from 2H16 on the back of increasing cement prices, we revise up our EPS forecasts from Rmb0.004 to Rmb0.026 in 16E (turning around from a loss in 15A), from Rmb0.050 to Rmb0.068 in 17E (+162% YoY) and from Rmb0.060 to Rmb0.078 in 18E (+15% YoY). We maintain our target price at HK\$1.20 and, with 26% upside, we maintain BUY.

Strong margin recovery in 2H16. As cement prices in Shaanxi Province have increased Rmb100/t since July, we expect WCC's average selling price (ASP) in 2H16 to reach Rmb305/t, increasing Rmb103/t HoH and Rmb100/t YoY. Although coal and other costs such as transportation cost largely increased in 2H16, we see the company's cooperation with Anhui Conch (914:HK – BUY) as likely to help reduce costs. We calculate its average costs at Rmb255/t, up Rmb79/t HoH and Rmb78/t YoY. Therefore, we forecast WCC's 2H16 unit margin at Rmb50/t, vs Rmb18/t in 1H16 and Rmb28/t in 2H15. As a result, we expect the full-year margin for 2016 to arrive at Rmb38/t.

Stable infrastructure demand in 2017. Shaanxi's demand largely depends on infrastructure construction, and especially that of railway and roads. However, due to insufficient funds, infrastructure construction has decelerated since 2H15, leading to a decline in regional cement prices. Recently, demand has picked up on the back of an increasing number of local high-speed railway and highway construction infrastructure projects. Notably, we expect the high-speed railway project around Xi'an to be the province's key infrastructure project for the next three years. We expect WCC to become one of the largest beneficiaries of increased cement demand for local projects and note that it has already signed to be the supplier for 10 expressway and eight railway projects, in addition to four power station projects in 2016-2020.

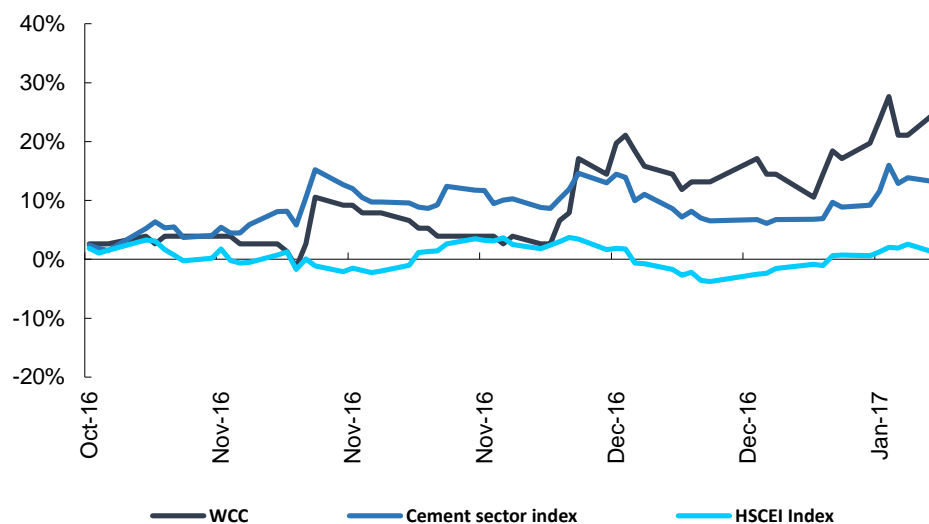
Potential M&A catalyst. Although Conch and WCC seem positive over a potential merger and acquisition (M&A), further details still need to be released as the current focus of the companies' partnership is on operations according to Conch. We expect a potential M&A case to reopen soon as the 12-month restriction to re-send a general offer will be lifted within less than five months. Conch currently holds 21.5% of WCC shares at an average price of HK\$1.59.

Maintain BUY. We remain upbeat on the potential for structural market changes and subsequent enhanced pricing power in Shaanxi. Given our expectation for higher margins from 2H16 on the back of increasing cement prices, we revise up our EPS forecasts from Rmb0.004 to Rmb0.026 in 16E (turning around from a loss in 15A), from Rmb0.050 to Rmb0.068 in 17E (+162% YoY) and from Rmb0.060 to Rmb0.078 in 18E (+15% YoY). We maintain our target price at HK\$1.20, representing a 16E EV/capacity of c.Rmb290/t. With 26% upside, we maintain BUY.

Preview of 2H16

West China Cement (WCC) stock price has increased c.21% since end-October, outperforming the Hong Kong Stock Exchange Hang Seng China Enterprises Index (HSCEI:IND) by c.18%. Given our expectation for higher margins from 2H16 on the back of increasing cement prices, we revise up our EPS forecasts from Rmb0.004 to Rmb0.026 in 16E (turning around from a loss in 15A), from Rmb0.050 to Rmb0.068 in 17E (+162% YoY) and from Rmb0.060 to Rmb0.078 in 18E (+15% YoY). We maintain our target price at HK\$1.20 and, with 30% upside, we maintain BUY.

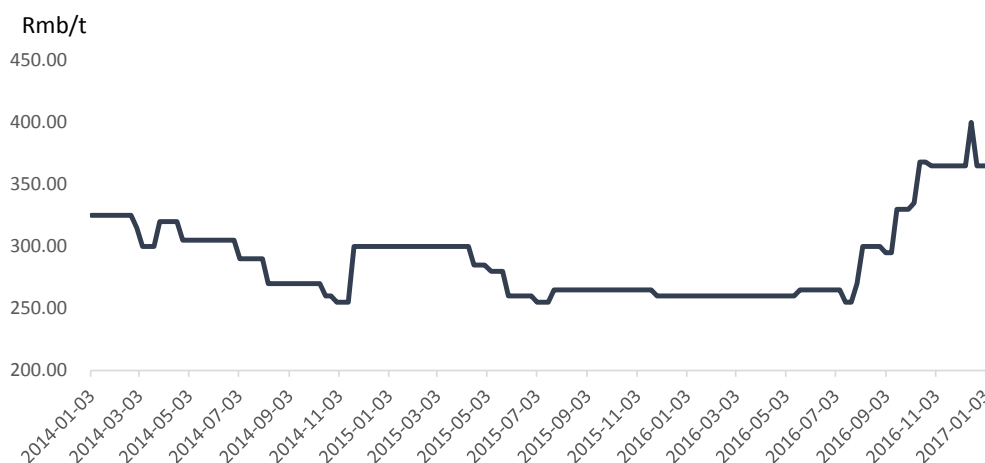
Fig 1: WCC stock performance in 4Q16



Source: Company, SWS Research

Strong margin recovery in 2H16. As cement prices in Shaanxi Province have increased Rmbxx/t since July, we expect WCC's average selling price (ASP) in 2H16 to reach Rmb305/t, increasing Rmb103/t HoH and Rmb100/t YoY. Although coal and other costs increased in 2H16, we see the company's cooperation with Anhui Conch (914:HK – BUY) as likely to help reduce costs. We calculate its average costs at Rmb255/t, up Rmb79/t HoH and Rmb78/t YoY. Therefore, we forecast WCC's 2H16 unit margin at Rmb50/t, vs Rmb18/t in 1H16 and Rmb28/t in 2H15. As a result, we expect the full-year margin for 2016 to arrive at Rmb38/t.

Fig 2: Shaanxi cement P.O 42.5 price from 2014-2017



Source: Company, SWS Research

Fig 3: Unit margin of 2H16 preview

| Rmb/t | 1H 2014 | 2H 2014 | 2014 | 1H2015 | 2H2015 | 1H2016 | 2H2016E | 2016E |
|-------------|---------|---------|--------|--------|--------|--------|---------|--------|
| Volume, 000 | 8,360 | 8,640 | 17,000 | 7,950 | 8,250 | 8,390 | 9,300 | 17,690 |
| ASP | 239 | 218 | 228 | 213 | 205 | 202 | 305 | 256 |
| ACP | -193 | -194 | -193 | -186 | -177 | -176 | -255 | -218 |
| GP | 46 | 25 | 35 | 27 | 28 | 18 | 50 | 38 |

Source: Company, SWS Research

Stable infrastructure demand in 2017. Shaanxi's demand largely depends on infrastructure construction, and especially that of railway and roads. However, due to insufficient funds, infrastructure construction has decelerated since 2H15, leading to a decline in regional cement prices. Recently, demand has picked up on the back of an increasing number of local high-speed railway and highway construction infrastructure projects. Notably, we expect the high-speed railway project around Xi'an to be the province's key infrastructure project for the next three years. We expect WCC to become one of the largest beneficiaries of increased cement demand for local projects and note that it has already signed to be the supplier for 10 expressway and eight railway projects, in addition to four power station projects in 2016-2020.

Fig 4: WCC key infrastructure projects

| WCC key infrastructure projects | | |
|--|------------------|-----------------------------|
| Project name | Estimated output | Planned construction period |
| Xi'an to Chengdu High Speed Railway Passenger Line | 3mt | 2012-2017 |
| Inner Mongolia to Jiangxi (Mengxi) Coal Transportation Railway | 0.9mt | 2016 |
| Hanjiang-To-Weihe River Water Transfer Project | N/A | 2020 |
| Ankang to Yangpingguan (Hanzhong City) Double Track Railway | 1.3mt | 2014-2016 |
| Baoji to Hanzhong Highway | 1mt | 2016 |
| Southern Shaanxi Resettlement Project | 0.3-0.4mt pa | 2011-2020 |

Source: Company, SWS Research

Fig 5: Other infrastructure projects

WCC other infrastructure projects

| Project Name | Planned construction period |
|---|-----------------------------|
| Expressway | |
| Pucheng-Baishui-Huangling Expressway | 2016-2020 |
| Taoba Expressway | 2016-2020 |
| National Route 312 Reconstruction | 2016-2020 |
| Shanyang to Zhashui Expressway(Group A) | 2016-2020 |
| Shanyang-Zhashui Expressway(Group of B,C,D) | 2016-2020 |
| Pingli-Zhenping Expressway | 2016-2020 |
| Xixiang-Zhenba Expressway | 2016-2020 |
| Wuqi-Dingbian Expressway | 2016-2020 |
| Suide-Yan'an Expressway | 2017-2020 |
| Airport | |
| Ankang Airport Project | 2016-2020 |
| Yan'an Airport | 2016-2020 |
| Xi'an Xianyang international Airport(phase III) | 2017-2020 |
| Railway | |
| Xi'an-Yinchuan Railway | 2016-2020 |
| Xi'an-Chongqing High-Speed Railway | 2017-2020 |
| Xi'an North Station | 2016-2020 |
| Xi'an-Wuhan High-Speed Railway | 2017-2020 |
| Xi'an-Yanan Intercity High-Speed Railway | 2017-2020 |
| Power Station | |
| Xunyang Hydropower Station | 2016-2020 |
| Zhenan Hydro-power Station | 2016-2020 |
| Shiquan Power Plant | 2016-2020 |

Source: Company, SWS Research

Potential M&A catalyst. Although Conch and WCC seem positive over a potential merger and acquisition (M&A), further details still need to be released as the current focus of the companies' partnership is on operations according to Conch. We expect a potential M&A case to reopen soon as the 12-month restriction to re-send a general offer will be lifted within less than five months. Conch currently holds 21.5% of WCC shares at an average price of HK\$1.59.

Fig 6: WCC largest shareholders

The Western Cement Primary Shareholder

| Shareholder | Stake |
|------------------------------------|--------|
| Jimin Zhang | 32.40% |
| Anhui Conch Cement Company Limited | 21.17% |
| Deutsche Bank Aktiengesellschaft | 5.39% |
| AllianceBernstein L.P. | 5.01% |

Source: Company, SWS Research

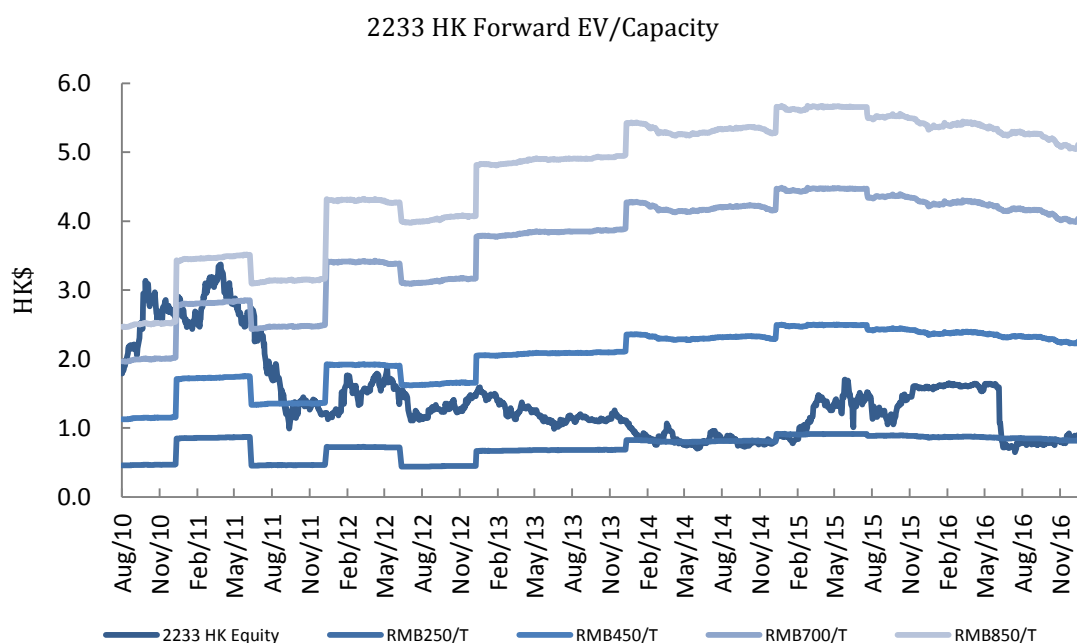
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Fig 7: Earnings forecast changes

| P&L | New | | Old | | Change | |
|-------------------|-------|--------|-------|-------|--------|-------|
| Year to Dec, Rmb | FY16E | FY17E | FY16E | FY17E | FY16E | FY17E |
| Volume, M T | 18.09 | 18.9 | 18.09 | 18.9 | 0.0% | 0.0% |
| Unit gross profit | 38 | 52 | 31 | 52 | 24.1% | 0.0% |
| Unit net profit | 8 | 19 | 1 | 15 | 594.7% | 33.3% |
| Net profit, Rmbm | 143 | 368 | 21 | 276 | 594.7% | 33.3% |
| EPS | 0.026 | 0.0680 | 0.004 | 0.051 | 594.7% | 33.3% |

Source: Company, SWS Research

Fig 8: WCC EV/t band



Source: Bloomberg, SWS Research

Table 1: Consolidated Income Statement

| Rmbm | 2014 | 2015 | 2016E | 2017E | 2018E |
|------|------|------|-------|-------|-------|
|------|------|------|-------|-------|-------|

| | | | | | |
|-------------------------|---------|---------|---------|---------|---------|
| Revenue | 3,883 | 3,501 | 4,631 | 5,009 | 5,152 |
| Cost of Sales | (3,285) | (3,037) | (3,935) | (4,158) | (4,277) |
| Gross Profit | 598 | 463 | 696 | 851 | 875 |
| Other Income | 53 | (188) | 36 | 151 | 156 |
| Distribution expenses | (36) | (43) | (46) | (48) | (50) |
| Administrative expenses | (258) | (271) | (271) | (284) | (292) |
| EBITDA | 956 | 609 | 1,256 | 1,749 | 1,941 |
| EBIT | 357 | (38) | 415 | 670 | 689 |
| Finance Costs | (222) | (218) | (217) | (208) | (156) |
| Profit before tax | 135 | (257) | 198 | 462 | 534 |
| Income tax expense | (96) | (51) | (51) | (92) | (107) |
| Minority interests | 4 | 2 | 4 | 1 | 2 |
| Profit for the year | 36 | (309) | 143 | 368 | 425 |

Source: Company, SWS Research

Table 2: Consolidated Cash Flow Statement

| Rmbm | 2014 | 2015 | 2016E | 2017E | 2018E |
|------------------------------------|-------|-------|-------|-------|-------|
| Profit before taxation | 135 | (257) | 198 | 462 | 534 |
| Plus : Depr. and amortisation | 626 | 703 | 662 | 635 | 609 |
| Finance cost | 227 | 237 | 217 | 208 | 156 |
| Losses from investments | 4 | 24 | 0 | 0 | 0 |
| Change in working capital | 179 | (391) | 105 | 8 | 19 |
| Others | (95) | (81) | (51) | (92) | (107) |
| CF from operating activities | 1,167 | 474 | 1,216 | 1,553 | 1,745 |
| CAPEX | (583) | (350) | (324) | (351) | (361) |
| Other CF from investing activities | (117) | 154 | 0 | 0 | 0 |
| CF from investing activities | (695) | (772) | (324) | (351) | (361) |
| Equity financing | 0 | 1,204 | 0 | 0 | 0 |
| Net change in liabilities | 2,531 | (287) | 0 | 0 | 0 |
| Dividend and interest paid | (442) | (272) | (246) | (282) | (241) |
| Other CF from financing activities | 1 | 0 | 4 | (40) | (39) |
| CF from financing activities | (483) | 255 | (242) | (322) | (279) |
| Net cash flow | (11) | (43) | 617 | 745 | 861 |
| FCFF | 484 | (127) | 932 | 1,191 | 1,313 |
| FCFE | 2,787 | (651) | 686 | 943 | 1,097 |

Source: Company, SWS Research

Table 3: Consolidated Balance Sheet

| Rmbm | 2014 | 2015 | 2016E | 2017E | 2018E |
|-----------------------------|--------|--------|--------|--------|--------|
| Current Assets | 1,857 | 2,042 | 2,362 | 3,401 | 4,565 |
| Bank balances and cash | 496 | 455 | 1,029 | 1,774 | 2,635 |
| Trade and other receivables | 601 | 685 | 717 | 775 | 797 |
| Inventories | 548 | 576 | 657 | 694 | 714 |
| Long-term investment | 39 | 54 | 0 | 50 | 0 |
| PP&E | 8,071 | 8,257 | 7,781 | 7,326 | 6,888 |
| Intangible and other assets | 1,052 | 1,157 | 1,035 | 1,068 | 1,005 |
| Total Assets | 10,768 | 11,382 | 11,104 | 11,723 | 12,384 |
| Current Liabilities | 2,362 | 2,770 | 2,987 | 3,091 | 3,152 |
| Borrowings | 745 | 538 | 538 | 538 | 538 |
| Trade and other payables | 1,598 | 1,411 | 1,628 | 1,732 | 1,793 |

| | | | | | |
|-------------------------------------|---------------|---------------|---------------|---------------|---------------|
| Other current liabilities | 3,326 | 3,527 | 3,527 | 3,527 | 3,527 |
| Long-term liabilities | 83 | 3 | 3 | 3 | 3 |
| Total Liabilities | 5,752 | 5,479 | 5,696 | 5,800 | 5,861 |
| Minority Interests | 46 | 47 | 51 | 52 | 54 |
| Shareholder Equity | 4,971 | 5,856 | 5,954 | 6,248 | 6,589 |
| Share Capital | 125 | 125 | 125 | 125 | 125 |
| Reserves | 0 | 0 | 0 | 0 | 0 |
| Equity attributable | 4,847 | 5,715 | 5,829 | 6,124 | 6,464 |
| Total Liabilities and equity | 10,768 | 11,382 | 11,104 | 11,723 | 12,384 |

Source: Company, SWS Research

Table 4: Key Financial Ratios

| | 2014 | 2015 | 2016E | 2017E | 2018E |
|--------------------------------|---------|----------|----------|--------|--------|
| Ratios per share (Rmb) | | | | | |
| Earnings per share | 0.01 | (0.06) | 0.0263 | 0.0680 | 0.0784 |
| Operating CF per share | 0.26 | 0.10 | 0.22 | 0.29 | 0.32 |
| Dividend per share | 0.00 | (0.01) | 0.01 | 0.01 | 0.02 |
| Net assets per share | 1.10 | 1.18 | 1.10 | 1.15 | 1.22 |
| Key Operating Ratios(%) | | | | | |
| ROIC | 4.08 | (0.44) | 6.08 | 10.69 | 12.82 |
| ROE | 0.72 | (5.24) | 4.29 | 10.13 | 11.46 |
| Gross profit margin | 15.40 | 13.24 | 15.03 | 16.98 | 16.98 |
| EBITDA Margin | 24.62 | 17.38 | 34.20 | 44.08 | 46.87 |
| EBIT Margin | 9.20 | (1.09) | 8.95 | 13.37 | 13.37 |
| Growth rate of Revenue(YoY) | (6.83) | (9.85) | 32.27 | 8.16 | 2.86 |
| Growth rate of Profit(YoY) | (90.51) | (961.25) | (146.14) | 158.23 | 15.36 |
| Debt-to-asset ratio | 0.08 | 0.05 | 0.05 | 0.05 | 0.04 |
| Turnover rate of net assets | 0.78 | 0.60 | 0.78 | 0.80 | 0.78 |
| Turnover rate of total assets | 0.36 | 0.31 | 0.39 | 0.47 | 0.53 |
| Effective tax rate (%) | 70.76 | (19.81) | 26.00 | 20.00 | 20.00 |
| Dividend yield (%) | 0.21 | (1.66) | 0.70 | 1.82 | 2.10 |
| Valuation Ratios (X) | | | | | |
| P/E | 95.7 | (12.2) | 28.8 | 11.2 | 9.7 |
| P/B | 0.7 | 0.6 | 0.7 | 0.7 | 0.6 |
| EV/Sales | 1.7 | 2.0 | 1.6 | 1.3 | 1.1 |
| EV/EBITDA | 6.3 | 10.4 | 4.8 | 3.0 | 2.3 |

Source: Company, SWS Research

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Introduction of Share Investment Rating

Security Investment Rating :

When measuring the difference between the markup of the security and that of the market's benchmark within six months after the release of this report, we define the terms as follows:

Trading BUY: Share price performance is expected to generate more than 20% upside over a 6-month period.

BUY: Share price performance is expected to generate more than 20% upside over a 12-month period.

Outperform: Share price performance is expected to generate between 10-20% upside over a 12-month period.

Hold: Share price performance is expected to generate between 10% downside to 10% upside over a 12-month period.

Underperform: Share price performance is expected to generate between 10-20% downside over a 12-month period.

SELL: Share price performance is expected to generate more than 20% downside over a 12-month period.

Industry Investment Rating:

When measuring the difference between the markup of the industry index and that of the market's benchmark within six months after the release of the report, we define the terms as follows:

Overweight : Industry performs better than that of the whole market :

Equal weight : Industry performs about the same as that of the whole market :

Underweight : Industry performs worse than that of the whole market.

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