

Company Report: China Railway Group (00390 HK)

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公司报告: 中国中铁 (00390 HK)

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Main Beneficiary of Urban Rail Transit Construction Boom, Maintain "Buy"

城轨建设繁荣潮的主要受益者, 维持“买入”

- China Railway Group's (00390 HK) 1H2020 revenue increased 15.0% YoY to RMB416.303 billion. Shareholders' profit increased 11.3% YoY to RMB11.697 billion. Results exceeded expectation, mainly due to stronger-than-expected recovery in infrastructure construction operation in 2Q2020. Overall gross margin decreased 0.9 ppts YoY to 8.7%. 1H2020 new contracts amounted to RMB870.34 billion, up 24.1% YoY.
- We expect total revenue to increase at a CAGR of 12.1% in 2019-2022 and expect overall gross margin to increase marginally from 9.1% in 2020 to 9.3% in 2022. In addition, we expect total expenses ratio to stay at approximately 3.9% in 2020-2022 and ROE to stay between 10.4% and 10.8% in 2020-2022.
- Our EPS estimates for 2020/ 2021/ 2022 are RMB0.960, RMB1.084 and RMB1.215, respectively. Due to the Government's increased attention to railway investment for fast-speed transportation consideration and environmental protection consideration, we expect railway investment to grow faster compared with other transportation investment such as highways and ports. In particular, urban rail transit investment will grow even faster, while the Company as the largest constructor will benefit the most. We maintain the TP at HK\$6.70, representing 4.6x/ 4.4x/ 4.1x 2020/ 2021/ 2022 EV/EBITDA. Maintain "Buy".
- 中国中铁(00390 HK)2020年上半年收入同比增15.0%至4,163.03亿元(人民币,下同)。股东净利同比增11.3%至116.97亿元。业绩超出预期,主要是由于公司基建建设业务2020年2季度复苏强于预期。公司整体毛利率同比下降0.9个百分点至8.7%。公司2020年上半年新签合同额达8,703.4亿元,同比上升24.1%。
- 我们预计2019-2022年整体收入将以12.1%的年复合增长率增长,预计整体毛利率将从2020年的9.1%上升至2022年的9.3%。此外,我们预计公司于2020-2022年间的总开支比率将维持在大约3.9%,2020-2022年间的净资产收益率则维持于10.4%至10.8%。
- 我们对于2020/2021/2022年的每股盈利预测分别为0.960元、1.084元及1.215元。鉴于政府出于更快速的交通及环境保护的考虑正在持续加大铁路投资的力度,我们预计铁路投资的增长将快于其他交通投资,例如公路及港口。而城轨投资的增长尤为迅速,公司作为最大的建设商将最为受惠。我们维持目标价为6.70港元,对应4.6/4.4/4.1倍2020/2021/2022年EV/EBITDA,维持“买入”评级。

Rating:

Buy

Maintained

评级:

买入 (维持)

6-18m TP 目标价:

HK\$6.70

Revised from 原目标价:

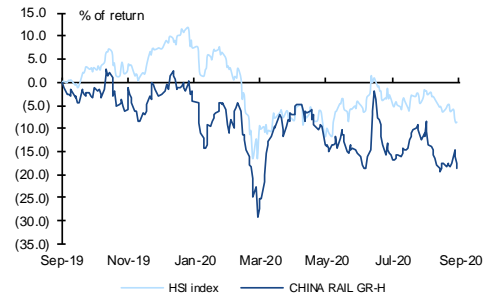
HK\$6.70

Share price 股价:

HK\$3.800

Stock performance

股价表现



Change in Share Price	1 M	3 M	1 Y
股价变动	1 个月	3 个月	1 年
Abs. % 绝对变动 %	(8.5)	(8.3)	(24.4)
Rel. % to HS Index 相对恒指变动 %	0.3	(2.3)	(13.1)
Avg. Share price(HK\$) 平均股价 (港元)	3.9	4.0	4.2

Source: Bloomberg, Guotai Junan International.

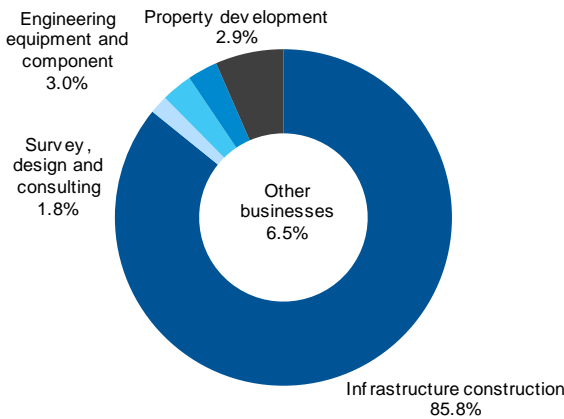
Year End	Turnover	Net Profit	EPS	EPS	PER	BPS	PBR	DPS	Yield	ROE
年结	收入	股东净利	每股净利	每股净利变动	市盈率	每股净资产	市净率	每股股息	股息率	净资产收益率
12/31	(RMB m)	(RMB m)	(RMB)	(Δ%)	(x)	(RMB)	(x)	(RMB)	(%)	(%)
2018A	740,383	16,409	0.718	7.3	4.6	9.717	0.3	0.128	3.8	9.0
2019A	850,843	22,119	0.950	32.3	3.6	10.540	0.3	0.169	5.0	10.7
2020F	979,083	23,598	0.960	1.1	3.5	11.441	0.3	0.176	5.3	10.4
2021F	1,090,604	26,634	1.084	12.9	3.1	13.078	0.3	0.199	5.9	10.6
2022F	1,197,242	29,850	1.215	12.1	2.8	14.804	0.2	0.222	6.6	10.8

Shares in issue (m) 总股数 (m)	24,570.9	Major shareholder 大股东	CRECG 47.2%
Market cap. (HK\$ m) 市值 (HK\$ m)	93,369.4	Free float (%) 自由流通比率 (%)	52.8
3 month average vol. 3 个月平均成交股数 ('000)	18,179.8	FY20 Net gearing (%) FY20 净负债/股东资金 (%)	42.0
52 Weeks high/low (HK\$) 52 周高/低 (HK\$)	5.100 / 3.450	FY20 Est. NAV (HK\$) FY20 每股估值 (港元)	8.5

Source: the Company, Guotai Junan International.

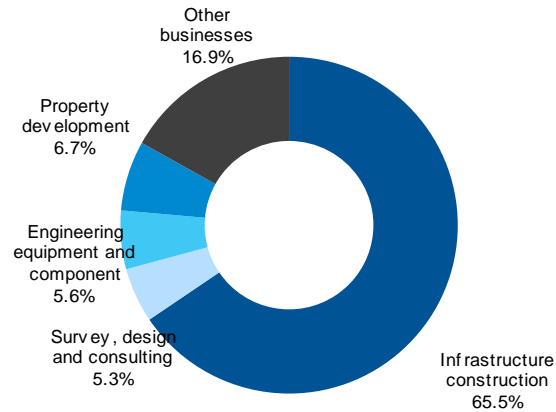
1H2020 shareholders' net profit increased 11.3% YoY to RMB11.697 billion; results exceeded expectations. China Railway Group's (00390 HK, CRG or the "Company") 1H2020 revenue increased 15.0% YoY to RMB416.303 billion. Shareholders' profit increased 11.3% YoY to RMB11.697 billion. EPS increased 6.5% YoY to 0.425. The growth rate of EPS was lower than that of shareholders' net profit due to the dilution effect of the Company's new share issuance in 2H2019. Results exceeded expectation, mainly due to stronger-than-expected recovery in infrastructure construction operation in 2Q2020. Overall gross margin decreased 0.9 pts YoY to 8.7%, mainly due to the increase in revenue contribution from low-gross margin infrastructure construction business, while gross margin of the infrastructure construction business actually stayed flat YoY at 7.1%, and didn't drop. Selling expense ratio decreased 0.1 pts YoY to 0.4%, administrative expenses ratio was down 0.4 pts YoY to 2.6%, and finance costs ratio decreased 0.2 pts YoY to 0.3%, costs ratio remained under control. 1H2020 new contracts amounted to RMB870.34 billion, up 24.1% YoY. In which infrastructure construction new contracts amounted to RMB758.70 billion, up 26.9% YoY.

Figure 1: CRG's Revenue by Segment in 1H2020



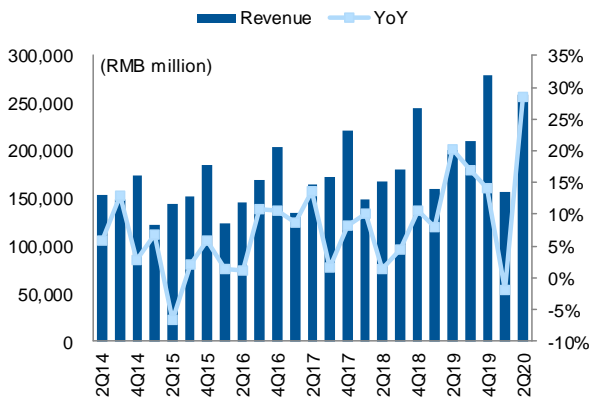
Source: the Company.

Figure 2: CRG's Gross Profit by Segment in 1H2020



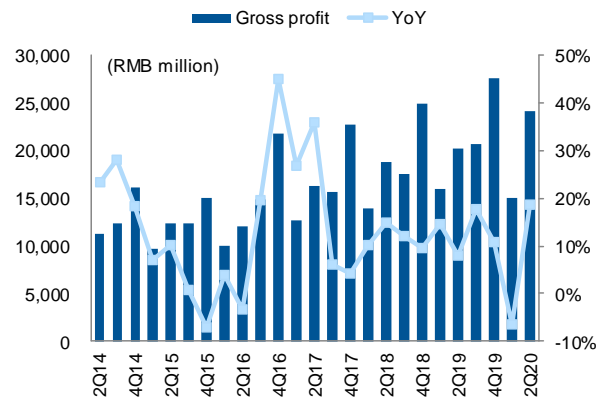
Source: the Company.

Figure 3: CRG's Quarterly Revenue

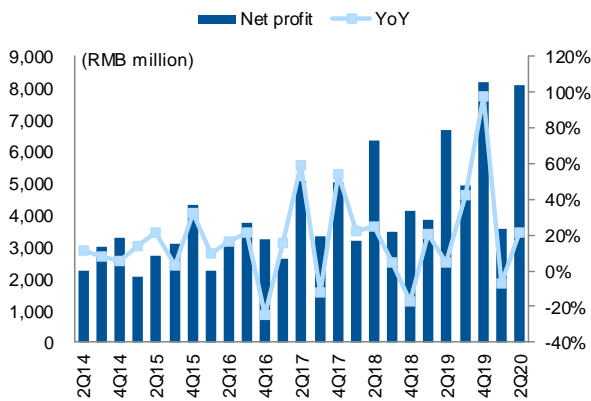


Source: the Company.

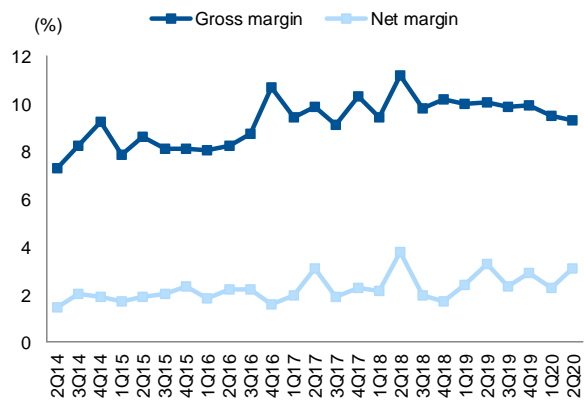
Figure 4: CRG's Quarterly Gross Profit



Source: the Company.

Figure 5: CRG's Net Profit


Source: the Company.

Figure 6: CRG's Quarterly Gross Margin and Net Margin (CAS)


Source: the Company.

Table 1: CRG's Segmental Performance in 1H2020

Segment (RMB Billion)	Revenue	YoY	Gross Margin (%)	YoY	New Contract	YoY
Infrastructure Construction	386	19.1%	7.1	0.0 ppts	759	26.9%
Survey, Design and Consulting Services	8	(0.1%)	27.6	0.9 ppts	11	(5.2%)
Engineering Equipment and Component Manufacturing	13	19.8%	17.6	(6.3 ppts)	19	20.3%
Property Development	13	(6.5%)	21.6	(9.0 ppts)	18	(27.8%)
Other Businesses	29	(4.3%)	24.0	0.2 ppts	63	24.4%
Inter-elimination	(33)	n.a.	n.a.	n.a.	n.a.	n.a.
Total	416	15.0%	8.7	(0.9 ppts)	870	24.1%

Source: the Company.

We expect total revenue to increase at a CAGR of 12.1% in 2019-2022. In 1H2020, total revenue increased 15.0% YoY to RMB416.303 billion, in which infrastructure construction revenue increased 19.1% YoY to RMB385.934 billion. According to the National Bureau of Statistics of China, Jan.-Aug. 2020 infrastructure investment growth was -0.3%, an improvement of 0.7 ppts from -1.0% in Jan.-Jul., while transportation, storage and postage investment increased 1.7% YoY, among which, railway investment and road investment were up 6.4% YoY and 2.9% YoY, respectively. We can see that transportation investment outperformed overall infrastructure investment while railway investment even outperformed road investment and average transportation investment. Under the "Outline of the Advanced Railway Planning for a Strong Country in the New Era" (August 2020), cities with population of 500,000 or above will have high-speed railway access by 2035, while HSR mileage should reach 70,000 km, approximately double the current 35,000 km; this suggests that HSR mileage will increase approximately by CAGR of 4.7% in 2020-2035, while ordinary railway mileage will increase from the current 104,000 km to 130,000 km by 2035, representing a CAGR of 1.4% in 2020-2035. Due to continued effort in urbanization and progress of regional development plans such as the "GD-HK-MA Greater Bay Area Development Plan", we expect investment growth for urban rail transit to remain high for at least 10 years and will be even faster than that of railways. In particular, the Company had a market share with over 50% in the fast-growing construction market in urban rail transit in China, and should outgrow its main peer China Railway Construction (01186 HK) in terms of construction revenue in 2020-2022. Considering all this, we expect construction revenue to increase at a CAGR of 12.9% in 2019-2022. As for survey, design and consultancy operations, manufacturing operations, real estate development operations and other businesses operations, we expect revenue CAGR of 10.0%, 13.0%, 3.3% and 6.3%, respectively, during 2019-2022. Overall, we expect total revenue to increase at a CAGR of 12.1% in 2019-2022.

We expect overall gross margin to be increase marginally from 9.1% in 2020 to 9.3% in 2022. In 1H2020, overall gross margin was down 0.9 ppts YoY to 8.7%, mainly due to the increase in revenue contribution from low-gross margin infrastructure construction business, while gross margin of the infrastructure construction business actually stayed flat YoY at 7.1%. In addition, gross profit from property development business dropped 34.0% YoY to only RMB2.8 billion, with a drop in revenue (down 6.5% YoY) and gross margin (down 9.0 ppts YoY). As the pandemic has been under control and the situation returned to normal in 2Q2020, we expect property development business to strongly recover and help to raise overall gross margin in

2H2020. Going forward, we expect construction gross margin to increase marginally from 2020 through 2022 with expected increase in construction revenue contribution from high-gross margin urban rail transit construction business, while gross margins of other business segments are likely to stay the same. Overall, we expect gross margin to increase marginally from 9.1% in 2020 to 9.3% in 2022.

We expect total expenses ratio to stay at approximately 3.9% in 2020-2022. In 1H2020, total expenses ratio (selling and distribution expenses, administrative expenses, R&D expenses and net finance costs) was at 3.3%, down 0.7 pts YoY. The substantial drop in total expenses ratio was mainly due to a stringent control for selling and administrative expenses under the COVID-19 pandemic period, while revenue recognition was not severely affected by the pandemic and maintained fast growth. Going forward, we expect selling expenses and administrative expenses to increase mostly in line with revenue due to the Company's stringent cost control KPI, and selling expenses ratio and administrative expenses ratio are likely to stay flat in 2020-2022. In addition, although the borrowings size is likely to increase from 2020 to 2022, the expected decrease in borrowing rate due to continuous relaxation in monetary policy is likely to keep overall interest expenses with little change, which will help to stabilize the net finance costs ratio. Overall, we expect total expenses ratio to stay at approximately 3.9% in 2020-2022.

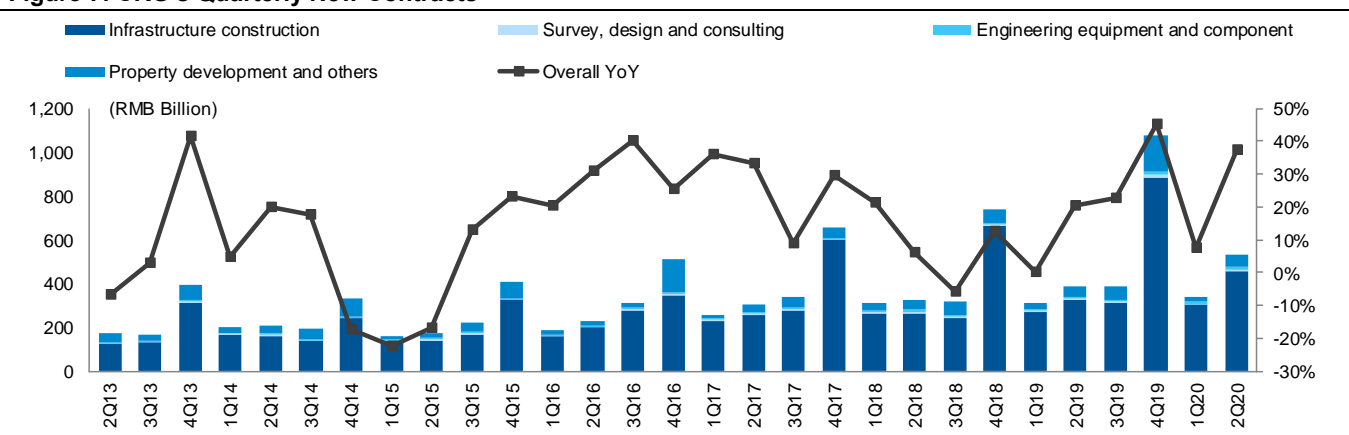
We expect the Company's ROE to stay between 10.4% and 10.8% in 2020-2022. We expect the net margin to stay approximately the same going forward due to expected little change in gross margin and total expenses ratio, as explained. In addition, we expect asset turnover to stay approximately the same as construction business should remain as the most significant revenue contributor with approximately 90% of revenue coming from that and asset turnover is likely to remain stable. Moreover, large SOEs such as the Company have had very strict KPI for debt control, and equity multiplier is unlikely to increase much. Overall, we expect the Company's ROE to stay between 10.4% and 10.8% in 2020-2022.

Table 2: CRG's Dupont Analysis

	2017A	2018A	2019A	2020F	2021F	2022F
Net Margin	2.3%	2.3%	2.8%	2.6%	2.6%	2.6%
Asset Turnover	0.8	0.8	0.8	0.8	0.8	0.8
Equity Multiplier	5.4	4.9	4.8	4.9	5.0	5.0
ROE	10.4%	9.0%	10.7%	10.4%	10.6%	10.8%

Source: the Company, Guotai Junan International.

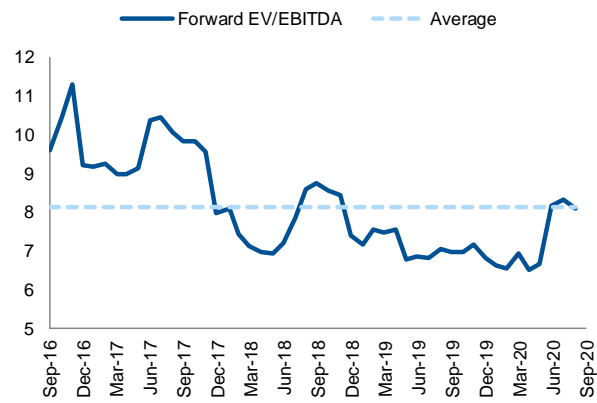
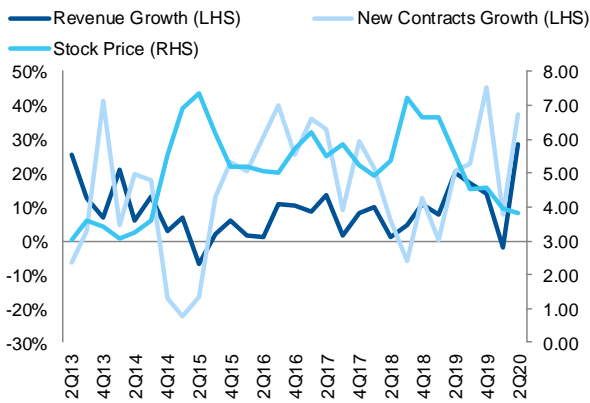
Figure 7: CRG's Quarterly New Contracts



Source: the Company.

Figure 8: CRG's Revenue Growth, Net Contracts Growth and Stock Prices

Figure 9: CRG's Forward EV/EBITDA



Source: the Company, Bloomberg.

Source: Bloomberg.

Maintain the TP at HK\$6.70, maintain "Buy". Our EPS estimates for 2020/ 2021/ 2022 are RMB0.960, RMB1.084 and RMB1.215, respectively. The Company recovered quickly in 2Q2020 from the impact from the COVID-19 pandemic in 1Q2020 and we expect growth of 6.2% in shareholders' net profit for full-year 2020. Going forward, due to the government's increased attention to railway investment for fast-speed transportation consideration and environmental protection consideration, we expect railway investment to grow faster compared with other transportation investment, such as for highways and ports. In addition, due to the construction of several city-cluster regions such as GD-HK-MA Greater Bay Area region and Beijing-Tianjin-Hebei region, we think that urban rail transit investment will maintain fast growth for at least the next 10 years. In particular, the Company's more focused approach in urban rail transit infrastructure construction business with over 50% of the construction market share in urban rail transit in China should mean that the Company will benefit the most from the expected infrastructure investment boom. We maintain the TP at HK\$6.70, representing 4.6x/ 4.4x/ 4.1x 2020/ 2021/ 2022 EV/EBITDA. Maintain "Buy".

Table 3: Peers Comparison

Company	Stock Code	Currency	Last price	Market cap(mn)	PE (fiscal year)				PB (fiscal year)				ROE(%) D/Y(%)	
					19A	20F	21F	22F	19A	20F	21F	22F	20F	20F
China Railway Group Ltd-H	390 HK	HKD	3.800	143,099	3.5	3.6	3.2	2.9	0.4	0.3	0.3	0.3	10.4	4.9
China Railway Construction-H	1186 HK	HKD	5.440	121,405	3.4	3.0	2.7	2.4	0.3	0.3	0.3	0.2	9.9	5.1
China Communications Const-H	1800 HK	HKD	4.120	118,333	3.1	3.2	2.8	2.6	0.3	0.2	0.2	0.2	7.8	6.1
China State Construction Int	3311 HK	HKD	5.310	26,054	5.0	4.4	3.8	3.4	0.6	0.5	0.5	0.5	12.7	6.9
China Railway Signal & Com-H	3969 HK	HKD	2.810	68,722	6.5	6.9	6.0	5.5	0.7	0.6	0.6	0.5	9.1	7.0
Metallurgical Corp Of Chin-H	1618 HK	HKD	1.270	58,957	4.1	3.2	2.8	2.6	0.3	0.2	0.2	0.2	3.6	7.3
China Energy Engineering C-H	3996 HK	HKD	0.730	21,946	3.8	4.2	3.7	3.1	0.4	0.3	0.3	0.3	7.7	4.7
Sinopec Engineering Group-H	2386 HK	HKD	3.160	13,550	5.7	5.4	4.9	4.6	0.5	0.4	0.4	0.4	8.3	11.0
China Machinery Engineerin-H	1829 HK	HKD	1.600	6,519	2.7	3.7	2.8	2.5	0.3	0.3	0.3	0.3	8.6	8.4
Simple Average					4.2	4.2	3.6	3.3	0.4	0.4	0.3	0.3	8.7	6.8
Weighted Average					4.0	3.8	3.4	3.1	0.4	0.3	0.3	0.3	8.8	6.0

Source: Bloomberg, Guotai Junan International.

Financial Statements and Ratios

Income Statement						Balance Sheet					
Year end 31 Dec (RMB m)	2018A	2019A	2020F	2021F	2022F	Year end 31 Dec (RMB m)	2018A	2019A	2020F	2021F	2022F
Total Revenue	740,383	850,843	979,083	1,090,604	1,197,242	Property, Plant and Equipment	64,687	68,383	66,932	68,144	69,214
Cost of Sales	(668,725)	(770,979)	(889,618)	(989,863)	(1,085,820)	Intangible Assets	46,200	25,559	28,115	30,926	34,019
Gross Profit	71,658	79,864	89,464	100,741	111,422	LT Receivables	26,487	44,612	48,377	52,483	56,964
Other Income and Gains	(17,507)	(13,317)	(13,049)	(15,516)	(17,278)	LT Investments	35,269	59,879	68,739	79,242	90,730
Selling and Distribution Expenses	(3,537)	(4,605)	(4,895)	(5,453)	(5,986)	Lease Prepayments	12,439	12,726	13,362	14,030	14,732
Administrative Expenses	(21,901)	(24,474)	(27,414)	(31,628)	(34,720)	Other Non-current Assets	105,391	135,112	155,358	173,403	191,494
Operating Profit	28,713	37,468	44,106	48,144	53,438	Total Non-current Assets	290,473	346,271	380,883	418,228	457,152
Finance Costs	(5,384)	(6,741)	(6,041)	(5,446)	(5,841)	Inventories	38,553	40,945	47,246	52,569	57,666
Share of Profits of Associates / JVs	1,616	2,460	1,866	2,053	2,258	Trade and Bills Receivables	212,392	203,256	233,891	260,532	286,007
Profit Before Tax	24,945	33,187	39,931	44,751	49,855	Contract Assets	122,947	130,155	149,772	166,832	183,144
Income Tax	(7,509)	(7,808)	(11,979)	(13,425)	(14,957)	Cash & Cash Equivalents	117,768	138,186	139,946	143,072	148,712
Profit After Tax	17,436	25,379	27,952	31,326	34,899	Other Current Assets	160,380	197,228	237,024	276,198	315,726
Non-controlling Interest	(1,027)	(3,260)	(4,354)	(4,692)	(5,049)	Total Current Assets	652,040	709,770	807,879	899,203	991,254
Shareholders' Profit / Loss	16,409	22,119	23,598	26,634	29,850	Total Assets	942,513	1,056,041	1,188,763	1,317,431	1,448,406
Basic EPS	0.718	0.950	0.960	1.084	1.215	Trade and Bills Payables	421,814	446,037	514,674	572,669	628,183
DPS	0.128	0.169	0.176	0.199	0.222	Contract Liabilities	91,999	110,370	121,407	133,548	146,902
						ST Borrowings	102,112	112,311	115,119	117,997	120,947
						Other Current Liabilities	6,550	7,316	8,283	9,141	9,973
						Total Current Liabilities	622,475	676,034	759,482	833,354	906,005
						LT Borrowings	88,808	118,934	130,827	143,910	158,301
						Other Non-current Liabilities	9,249	15,745	17,329	18,830	20,361
						Total Non-current Liabilities	98,057	134,679	148,157	162,740	178,662
						Total Liabilities	720,532	810,713	907,639	996,095	1,084,667
						Total Shareholders' Equity	159,510	189,775	210,618	233,924	259,869
						Minority Interest	62,471	55,553	70,506	87,412	103,869
						Total Equity	221,981	245,328	281,124	321,336	363,738
						Total Equity and Liabilities	942,513	1,056,041	1,188,763	1,317,431	1,448,406
						BVPS	9.717	10.540	11.441	13.078	14.804

Cash Flow Statement					
Year end 31 Dec (RMB m)	2018A	2019A	2020F	2021F	2022F
Profit Before Tax	24,945	33,187	39,931	44,751	49,855
Depreciation and Amortization	9,875	11,565	10,316	10,916	11,521
Change in Working Capitals	(24,738)	(19,440)	(27,324)	(26,996)	(25,547)
Other Operating Activities	1,880	(3,114)	1,921	(504)	(1,895)
Cash from Operating Activities	11,962	22,198	24,843	28,167	33,934
Capital Expenditure	(18,842)	(19,838)	(18,774)	(20,925)	(20,528)
Other Investing Activities	(20,491)	(20,341)	(13,544)	(14,914)	(16,647)
Cash from Investing Activities	(39,333)	(40,179)	(32,317)	(35,839)	(37,176)
Net Borrowings	6,093	32,622	14,701	15,961	17,341
Interests	(8,405)	(10,464)	(8,351)	(7,872)	(8,388)
Dividends	(4,224)	(5,575)	(5,711)	(5,873)	(6,446)
Other Financing Activities	34,443	21,632	8,515	8,311	6,196
Cash from Financing Activities	27,907	38,215	9,153	10,527	8,703
Cash at Beg of Year	116,688	117,768	138,186	139,946	143,072
Net Changes in Cash	536	20,234	1,679	2,855	5,462
Forex Changes	544	184	81	270	178
Cash at End of Year	117,768	138,186	139,946	143,072	148,712

Financial Ratios					
	2018A	2019A	2020F	2021F	2022F
Gross Margin (%)	9.7	9.4	9.1	9.2	9.3
Operating Margin (%)	3.9	4.4	4.5	4.4	4.5
Net Margin (%)	2.3	2.8	2.6	2.6	2.6
ROA (%)	1.9	2.4	2.2	2.2	2.3
ROE (%)	9.0	10.7	10.4	10.6	10.8
Net Gearing Ratio (%)	37.3	41.8	42.0	42.6	42.1
Interest Coverage (x)	4.0	4.2	5.3	6.1	6.4

Source: the Company, Guotai Junan International.

Company Rating Definition

The Benchmark: Hong Kong Hang Seng Index

Time Horizon: 6 to 18 months

Rating		Definition
Buy	买入	Relative Performance > 15%; or the fundamental outlook of the company or sector is favorable.
Accumulate	收集	Relative Performance is 5% to 15%; or the fundamental outlook of the company or sector is favorable.
Neutral	中性	Relative Performance is -5% to 5%; or the fundamental outlook of the company or sector is neutral.
Reduce	减持	Relative Performance is -5% to -15%; or the fundamental outlook of the company or sector is unfavorable.
Sell	卖出	Relative Performance < -15%; or the fundamental outlook of the company or sector is unfavorable.

Sector Rating Definition

The Benchmark: Hong Kong Hang Seng Index

Time Horizon: 6 to 18 months

Rating		Definition
Outperform	跑赢大市	Relative Performance > 5%; or the fundamental outlook of the sector is favorable.
Neutral	中性	Relative Performance is -5% to 5%; or the fundamental outlook of the sector is neutral.
Underperform	跑输大市	Relative Performance < -5%; Or the fundamental outlook of the sector is unfavorable.

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