



Company Report: Shanghai Electric (02727 HK)

公司报告: 上海电气 (02727 HK)

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1H2018 Earnings Increased 12.5% YoY, Upgrade to "Buy"

2018上半年盈利同比增12.5%，上调至“买入”

- **1H2018 earnings went up YoY by 12.5%, beating expectations.** Sales and net profit in 1H2018 went up YoY by 24.4% and 12.5%, respectively. Gross margin for the period went down YoY by 2.3 ppt to 17.1% and net margin was down YoY by 0.4 ppt to 3.4%. Results were better than expectations.
- **New orders in the first 6 months went up YoY by 20.8%.** New orders signed in 1H2018 reached RMB 66.53 bn, up YoY by 20.8%, and orders on hand reached RMB 226.1 bn (including RMB 104.6 bn in orders not yet coming into effect), which was relatively flat compared to that at year end 2017. New orders of modern services grew 68.6% YoY to RMB 28.6 bn and became the key contributor of new orders growth.
- **Power generating infrastructure investment in China in 7M2018 reached RMB 123.8 bn, down YoY by 1.3%.** In 7M2018, newly installed power capacity in China reached 66.6 GW, down YoY by 3.2%. Newly installed thermal and hydro during the period dropped YoY by 0.2% and 28.4%, respectively. However, newly installed wind capacity increased 46.9% YoY in 1H2018. We expect China's investment in thermal and hydro power to continue their current downtrend while China's investment in wind, nuclear and solar energies will accelerate.
- **We upgrade the rating to "Buy" and raise the TP to HK\$ 3.63.** We maintain our bullish view on Shanghai Electric given its continued reform and transformation as well as its solid operating performance in 1H2018. Our TP corresponds to 15.0x/ 13.3x/ 12.3x FY18-FY20 PER or 0.8x/ 0.8x/ 0.8x FY18-FY20 PBR.
- **2018上半年盈利同比上涨12.5%，好于预期。**公司于期内的销售额和净利润分别同比增长24.4%和12.5%。毛利率同比下降2.3个百分点至17.1%，而净利率亦同比下滑0.4个百分点至3.4%。期内业绩好于预期。
- **今年前6个月的新增订单同比上升20.8%。**公司在2018上半年的新签订单达665.3亿人民币，同比上升20.8%，期末在手订单达到2,261亿人民币（其中尚未生效订单达1,046亿人民币），与2017年底时的水平相若。现代服务的新订单同比增68.6%至人民币286亿，是期内新增订单增长的主要贡献者。
- **国内于2018年前7个月对发电基础设施的投资同比降1.3%至人民币1,238亿。**国内于2018年1-7月的新增发电装机容量达66.6吉瓦，同比下滑3.2%。期内新增火电及水电分别同比下降0.2%及28.4%，但期内新增风电则同比上升了46.9%。我们预计国内对火电及水电的投资将持续当前的下行趋势，但将加快对风能、核能及太阳能的投资。
- **我们上调投资评级至“买入”，目标价上调为3.63港元。**鉴于上海电气的持续改革和转型以及其上半年不俗的业绩，我们维持对上海电气的乐观的看法。我们的目标价相当于15.0倍/13.3倍/12.3倍的2018-2020年市盈率或0.8倍/0.8倍/0.8倍2018-2020市净率。

Rating:

Buy

Upgraded

评级:

买入 (上调)

6-18m TP 目标价:

HK\$3.63

Revised from 原目标价:

HK\$3.56

Share price 股价:

HK\$2.450

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 %	(2.8)	(18.9)	(28.8)
Rel. % to HS Index 相对恒指变动 %	(3.9)	(9.1)	(29.6)
Avg. share price (HK\$) 平均股价 (港元)	2.52	2.58	2.89

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)	(%)	(%)
2016A	88,507	2,355	0.171	7.7	12.8	3.566	0.6	0.000	0.0	5.4
2017A	79,544	2,627	0.187	9.2	10.9	3.772	0.5	0.092	4.5	5.1
2018F	99,325	3,062	0.208	11.1	10.1	3.758	0.6	0.083	3.9	5.5
2019F	110,991	3,448	0.234	12.6	9.0	3.772	0.6	0.082	3.9	6.2
2020F	120,525	3,733	0.253	8.3	8.3	3.800	0.6	0.089	4.2	6.7
Shares in issue (m) 总股数 (m)				14,725.2	Major shareholder 大股东				SEC Group	60.8%
Market cap. (HK\$ m) 市值 (HK\$ m)				36,076.7	Free float (%) 自由流通比率 (%)					35.8
3 month average vol. 3个月平均成交股数 ('000)				8,657.8	FY18 Net gearing (%) FY18 净负债/股东资金 (%)					Net Cash
52 Weeks high/low (HK\$) 52周高/低				3.700 / 2.380	FY18 EV / EBITDA (x) FY18 企业值 / EBITDA (x)					5.1

Source: the Company, Guotai Junan International.

Earnings in 1H2018 went up YoY by 12.5% to RMB 1,764 mn, beating expectation. The Company's net earnings during the period were better than both the market expectation and our expectation. During the first 6 months, sales and net profit went up YoY by 24.4% and 12.5%, respectively. Sales of all business segments experienced dramatic growth during the reporting period, in which sales of new energy & environmental protection equipment grew 34.2% YoY to RMB 6.6 bn, sales of high efficiency clean energy equipment grew 32.4% YoY to RMB 15.2 bn, sales of industrial equipment grew 12.6% YoY to RMB 18.1 bn, sales of modern services grew 22.9% YoY to RMB 9.5 bn, and sales of other businesses grew 84.0% YoY to RMB 1.8 bn. The dramatic growth can be attributable to the 2nd round of corporate restructuring completed in November 2017, wherein the Company issued new A-shares and purchased a bunch of new assets from its parent, Shanghai Electric Group. During the reporting period, except for the 1.1 ppt increase in the gross margin of modern services segment, gross margin of all other segments experienced declines (high efficiency & clean energy equipment segment gross margin dropped by 2.8 pts due to the thermal downtrend). The Company's overall gross margin in 1H2018 went down by 2.3 pts YoY to 17.1% and net margin declined 0.4 ppt YoY to 3.4%. Looking ahead, we believe Shanghai Electric will continue to benefit from further SOE reform (restructuring, management improvement, etc.), Belt and Road strategy, and continued corporation transformation via M&As. We remain optimistic about the outlook of Shanghai Electric.

Table-1: 1H2018 Operating Results and YoY Comparison

(RMB mn)	1H2018	1H2017 (Restated)	YoY Δ	Comments
Revenue	51,274.0	41,224.3	24.4%	All business segments recorded YoY increase in sales during the period
COGS	(42,493.4)	(33,222.3)	27.9%	
Gross profit	8,780.6	8,002.1	9.7%	Due to gross margin decline of 2.3 pts
Selling expense	(1,264.1)	(1,129.3)	11.9%	
General & admin expense	(5,012.7)	(4,719.8)	6.2%	Impairment loss on financial assets reached RMB 541 mn in 1H2018
EBIT	2,503.7	2,153.0	16.3%	
Other income and gains	570.7	396.6	43.9%	
Finance income / (cost)	(339.3)	(209.1)	62.3%	
Share of affiliate / JV	507.3	601.8	-15.7%	
Profit before tax	3,242.5	2,942.3	10.2%	
Income tax	(311.3)	(350.9)	-11.3%	
Minority interest	(1,167.2)	(1,023.9)	14.0%	
Net income	1,764.0	1,567.4	12.5%	
EPS (Basic)	0.1198	0.1125	6.5%	
Margins (YoY)			YoY ppt Δ	
Gross margin	17.1%	19.4%	-2.3 ppt	Gross margin in 3 out of 4 business segments experienced YoY decline, mainly due to sharp rise in raw materials price (i.e. steel)
EBIT margin	4.9%	5.2%	-0.3 ppt	
PBT margin	6.3%	7.1%	-0.8 ppt	
Net margin	3.4%	3.8%	-0.4 ppt	

Source: the Company, Guotai Junan International.

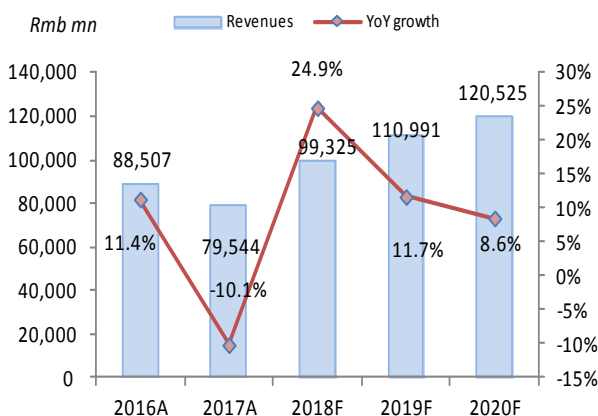
New orders in the first half of 2018 went up by 20.8% YoY to RMB 66.53 bn. New orders obtained during the reporting period reached RMB 66.53 bn, up YoY by 20.8%, in which new orders from new energy & environmental protection equipment, high efficiency & clean energy equipment, industrial equipment and modern services accounted for 11.5%, 11.4%, 34.2% and 42.9% of total new orders, respectively. New orders of modern services and of industrial equipment grew YoY by 68.6% and 18.8% to RMB 28.6 bn and RMB 22.8 bn in 1H2018, respectively. However, new orders of high efficiency & clean energy equipment dropped YoY by 35.2% to RMB 7.56 bn due to the thermal downtrend in the domestic market. In 1H2018, new orders of environmental protection equipment went up 187.3% to RMB 2.3 bn, while that of overseas power plant engineering went up 28.6% to RMB 18.8 bn. Orders on hand amounted to RMB 226.1 bn by the end of 1H2018 (including orders in the amount of RMB 104.6 bn not yet coming into effect), which remained at the same level compared to the end of 2017. New energy & environmental protection equipment, high efficiency & clean energy equipment, industrial equipment and modern services accounted for 14.5%, 40.0%, 5.6% and 39.9% of total orders on hand, respectively. Coal fired power equipment added only RMB 430 mn in new orders during the first 6 months but still contributed RMB 6.6 bn in orders on hand. Risks of order cancellations and indefinite postponement of delivery of thermal equipment orders are still quite high given the existing thermal downtrend in China with specific policy aiming to curb its development during the 13th Five-Year period. Nationwide thermal power installed capacity shall be no more than 1,100 GW by 2020. Looking ahead, we expect new energy equipment, industrial equipment and modern services to drive the growth of Shanghai Electric's new orders amid the expected decline in new orders of high efficiency & clean energy equipment (mainly composed of coal-fired power equipment).

Power generating infrastructure investment in China in 7M2018 reached RMB 123.8 bn, down YoY by 1.3%. According to CEC, nationwide newly installed power generating capacity in 7M2018 reached 66.6 GW, down YoY by 3.2% or YoY decrement of 2.2 GW. Thermal, hydro, nuclear, wind and solar contributed 18.8 GW, 4.8 GW, 2.2 GW, 9.5 GW and 31.3 GW, respectively, of newly installed capacity in 7M2018. Wind and nuclear power new installations went up YoY by 29.6% and 103.5%, respectively, while thermal, hydro and solar new installations went down YoY by 0.2%, 28.4% and 10.5%, respectively. Nationwide power generating infrastructure investment in 7M2018 reached RMB 123.8 bn, down YoY by 1.3%. Thermal, hydro, nuclear and wind power investment in 7M2018 went up YoY by 1.9%, 17.8%, 11.2% and down YoY by 4.9%, respectively. During the first 7 months in 2018, renewable energies such as hydro, nuclear and wind power contributed 69.2% of power generating infrastructure investment in China. Meanwhile, nationwide power grid investment reached RMB 234.7 bn in 7M2018, down YoY by 16.6%. Power generating infrastructure investment remained stable while the investment on power grid continued to decline in the first 7 months. However, we expect the investment on power grid to accelerate in the remaining 5 months of 2018 with total nationwide spending on power grid expected to exceed RMB 500 bn again in 2018.

We raise our earnings forecasts based on optimistic assumptions on the outlook of Shanghai Electric. The Company completed its second round of restructuring with its parent (Shanghai Electric Group) in November 2017 with the placing of approximately 1.3 bn new A-shares in acquiring new assets from its parent and in securing approximately RMB 3 bn in new capital funding. Following an impressive operation in 1H2018, we expect the strong revenues growth to continue in the second half of 2018, but the growth rate is expected to slow down in 2019 and 2020. We expect sales growth to be 24.9%/ 11.7%/ 8.6% from 2018 to 2020, respectively. Meanwhile, we expect overall gross margin to gradually recover and is estimated to be 17.2%/ 17.9%/ 18.2% from 2018 to 2020, respectively. We believe that the Company will continue to improve its profitability via continued transformation and management improvement. We believe that the increased risk in the Company's thermal power equipment segment will somehow be offset by the new businesses injected to the Company from the two rounds of corporate restructuring completed. The Company will continue to transform itself with the establishment of new business ventures and with the merger & acquisition on promising assets. The Company has been eyeing to enter the solar industry and has almost reached a deal with GCL Poly Energy (03800.HK) to acquire the latter's operating subsidiary, Jiangsu Zhongneng, before the deal was called off due to many reasons including valuation and deal structure. However, the Company is quite bullish on the solar industry and guided that it may one day enter the solar industry when the existing uncertainties become clearer. Adding a solar business venture would dramatically beef up the scale and earnings contribution of the new energy segment as well as further transform Shanghai Electric. We expect the fundamentals of Company to remain solid in the years to come and in our forecast period given Shanghai Electric's continued transformation. Our EPS estimates from FY18 to FY20 are RMB 0.208, RMB 0.234 and RMB 0.253, respectively.

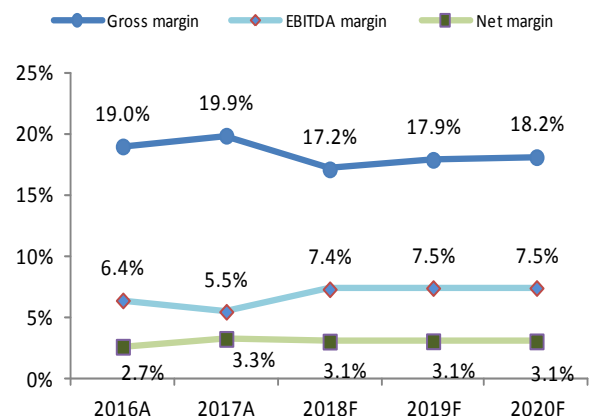
We raise the investing rating to "Buy" and the TP to HK\$ 3.63. We expect Shanghai Electric to benefit from the continued SOE reforms, the increased earnings contribution from the new assets purchased from its parent, and the growing requirement for environmental protection in the domestic market (leading to increased spending in renewable energy and rise in demand for environmental protection equipment & services). We thus raise our rating to "Buy" and revise up our TP to HK\$ 3.63. Our TP corresponds to 15.0x/ 13.3x/ 12.3x FY18-FY20 PER or 0.8x/ 0.8x/ 0.8x FY18-FY20 PBR.

Figure-1: Historical & Projected Revenues



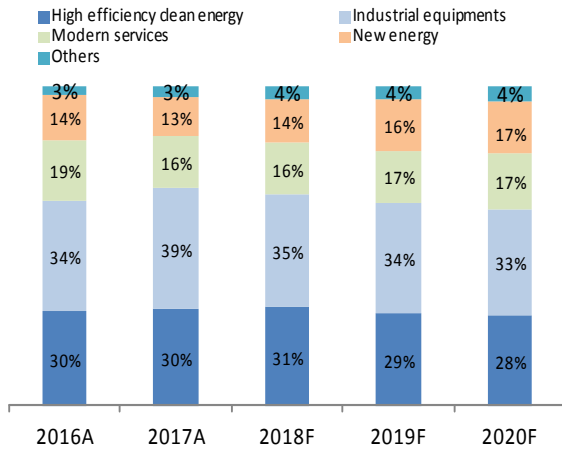
Source: the Company, Guotai Junan International.

Figure-2: Margin Analysis



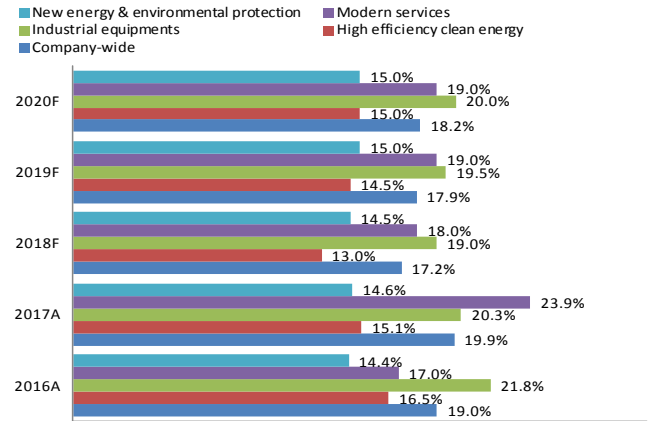
Source: the Company, Guotai Junan International.

Figure-3: Historical & Projected Revenue Breakdown



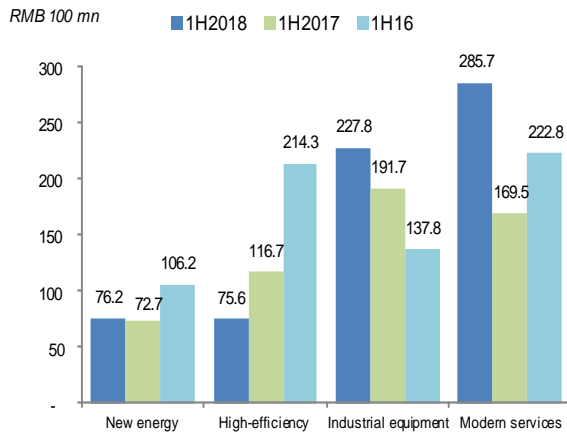
Source: the Company, Guotai Junan International.

Figure-4: Historical Gross Margin Breakdown



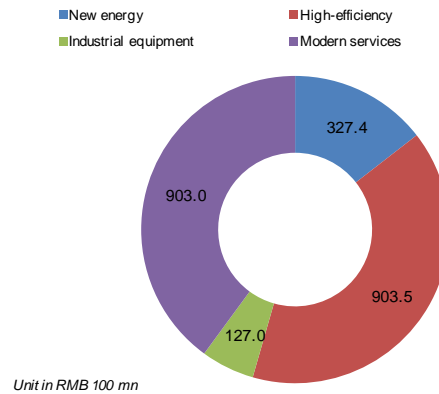
Source: the Company, Guotai Junan International.

Figure-5: 6M2018 New Orders Breakdown



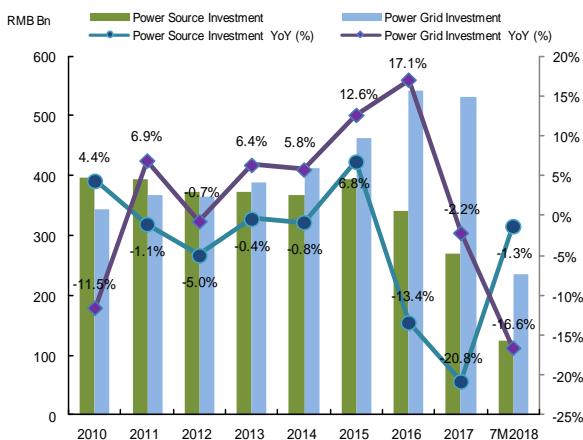
Source: the Company, Guotai Junan International.

Figure-6: 6M2018 Orders Backlog Breakdown



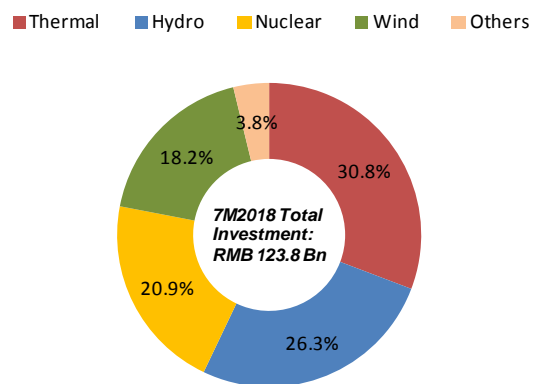
Source: the Company, Guotai Junan International.

Figure-7: Historical Power Sector Investment in PRC

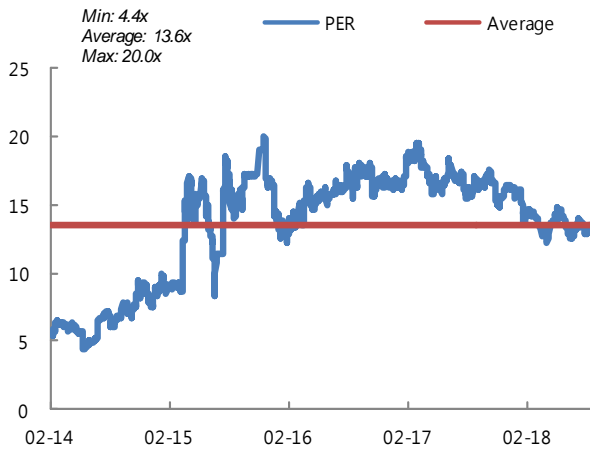


Source: NEA, Guotai Junan International.

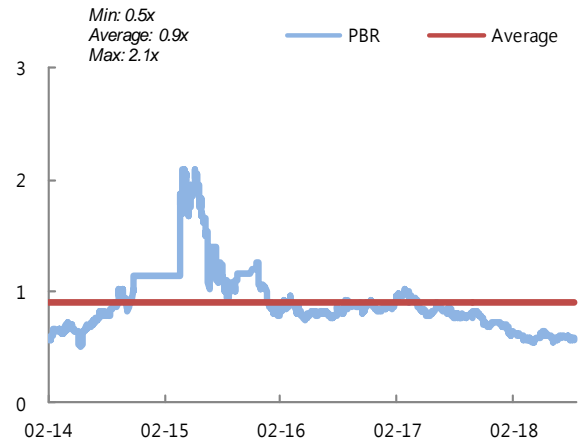
Figure-8: 7M2018 Power Infrastructure Investment in PRC



Source: NEA, Guotai Junan International.

Figure-9: Forward PER of Shanghai Electric


Source: Bloomberg, Guotai Junan International.

Figure-10: Forward PBR of Shanghai Electric


Source: Bloomberg, Guotai Junan International.

Table-2: Peers Comparison

Company	Stock Code	Currency	Last price (in local \$)	PE (fiscal year)				PB (fiscal year)				ROE (%)	ROA (%)	Market Cap HKD mn
				17A	18F	19F	20F	17A	18F	19F	20F	18F	18F	
HK - Listed Peers														
Dongfang Electric Corp - H	01072 HK	HKD	4.37	13.1	11.3	11.2	12.3	0.4	0.5	0.4	0.4	3.9	1.1	24,270
Harbin Electric	01133 HK	HKD	2.43	15.0	25.9	14.7	14.2	0.2	0.2	0.2	0.2	3.7	n.a.	3,346
Shanghai Electric - H	02727 HK	HKD	2.45	11.3	13.1	13.2	12.6	0.5	0.6	0.5	0.5	4.5	1.2	73,572
Xinjiang Goldwind	02208 HK	HKD	8.46	8.7	7.9	7.6	7.2	1.1	1.1	1.0	0.9	14.3	4.6	47,231
Simple Average				12.0	14.5	11.7	11.6	0.6	0.6	0.5	0.5	6.6	2.3	
Weighted Average				10.9	11.4	11.1	10.8	0.7	0.7	0.6	0.6	7.5	2.3	
Offshore - Listed Peers														
Alstom	ALO.FP	EUR	37.71	28.6	17.5	18.2	18.0	2.3	2.1	2.3	2.2	12.5	3.3	76,103
Bharat Heavy Electricals	BHEL	INR	78.05	n.a.	n.a.	23.2	18.4	0.9	0.9	0.9	0.8	1.4	0.7	31,423
Doosan Heavy Industries	034020 KS	KRW	14,300.00	n.a.	23.6	8.6	6.4	0.5	0.5	0.5	0.4	2.6	1.3	11,772
General Electric	GE US	USD	12.94	n.a.	13.9	12.4	10.9	1.7	2.6	2.9	2.7	12.8	1.0	882,753
Hyundai Heavy Industries	009540 KS	KRW	118,500.00	2.6	n.a.	n.a.	22.0	0.6	0.7	0.7	0.6	(1.6)	(0.8)	57,597
Mitsubishi Heavy Industries	7011 JT	JPY	4,104.00	15.7	19.6	16.7	12.8	0.8	0.8	0.8	0.7	3.9	1.3	97,573
Siemens Ag	SIE GY	EUR	110.50	14.9	15.0	13.9	12.5	2.1	2.0	1.9	1.7	13.1	4.3	852,624
Wartsila Oyj Abp	WRT1V FH	EUR	17.86	27.5	21.0	17.7	15.9	4.5	4.2	3.7	3.3	20.2	10.1	95,935
Simple Average				17.9	18.4	15.8	14.6	1.7	1.7	1.7	1.6	8.1	2.7	
Weighted Average				16.2	15.2	13.8	12.5	1.9	2.2	2.3	2.1	12.2	2.8	

 Source: Bloomberg, Guotai Junan International. Prices as at September 4th, 2018.

Financial Statements and Ratios

Income Statement						Balance Sheet					
Year end 31 Dec (RMB m)	2016A	2017A	2018F	2019F	2020F	Year end 31 Dec (RMB m)	2016A	2017A	2018F	2019F	2020F
Total Revenue	88,507	79,544	99,325	110,991	120,525	PPE	15,501	16,469	19,018	23,045	27,312
COGS	(71,657)	(63,702)	(82,277)	(91,074)	(98,635)	Investment in affiliates	9,264	10,705	11,990	12,589	13,218
Gross profit	16,850	15,842	17,049	19,916	21,890	Intangible & goodwill	3,976	4,042	5,481	6,990	8,638
Selling expense	(2,553)	(2,254)	(2,433)	(2,775)	(3,073)	Other non-current assets	20,186	23,773	19,570	21,468	23,078
Admin expense	(10,482)	(11,447)	(9,734)	(11,488)	(12,655)	Total Non-current Assets	48,927	54,988	56,059	64,091	72,247
Operating Profit	3,815	2,141	4,881	5,654	6,161	Cash & Cash Equivalents	40,917	33,391	34,158	35,517	33,747
Other income	1,639	2,340	1,170	1,228	1,290	Inventories	22,185	29,057	31,265	36,430	39,454
Gain from affiliates & JVs	826	1,342	1,007	1,057	1,110	Trade receivable	44,034	49,148	54,629	55,495	57,852
Finance income	(354)	(458)	(666)	(838)	(959)	Other current assets	30,538	32,761	27,036	30,581	34,079
Profit Before Tax	5,925	5,365	6,392	7,101	7,602	Total Current Assets	137,674	144,357	147,087	158,023	165,131
Income Tax	(1,283)	(522)	(1,003)	(1,210)	(1,304)	Total Assets	186,601	199,346	203,146	222,114	237,378
Profit After Tax	4,642	4,843	5,389	5,891	6,298	Short-term debts	2,582	3,224	8,436	9,056	7,461
Non-controlling Interest	(2,288)	(2,216)	(2,327)	(2,443)	(2,565)	Bonds, ST	499	1,600	0	0	0
Shareholders' Profit / Loss	2,355	2,627	3,062	3,448	3,733	Trade payable	38,543	40,885	41,138	45,537	49,317
Basic EPS (RMB)	0.171	0.187	0.208	0.234	0.253	Advances & deposits	46,587	47,425	41,717	46,616	50,620
DPS (RMB)	0.000	0.092	0.083	0.082	0.089	Others	18,164	18,186	18,770	20,457	21,832
						Total Current Liabilities	106,375	111,320	110,061	121,666	129,231
						Long-term debts	3,371	4,144	6,694	9,194	10,694
						Corporate bond	11,148	10,058	10,258	12,258	15,258
						Others	3,288	3,102	3,291	3,496	3,714
						Total Non-current Liabilities	17,807	17,304	20,243	24,948	29,666
						Total Liabilities	124,182	128,624	130,304	146,614	158,897
						Total Shareholders' Equity	47,900	55,537	55,331	55,545	55,961
						Minority Interest	14,519	15,185	17,511	19,955	22,520
						Total Equity	62,419	70,722	72,842	75,500	78,481
						BPS (RMB)	3.566	3.772	3.758	3.772	3.800

Cash Flow Statement					
Year end 31 Dec (RMB m)	2016A	2017A	2018F	2019F	2020F
Operating activities					
Net income	2,355	2,627	3,062	3,448	3,733
D&A	1,891	2,249	2,429	2,623	2,833
Change in working capital	4,377	(11,904)	(5,497)	1,176	90
Others	2,093	(496)	401	397	412
Cash from Operating Activities	10,716	(7,525)	395	7,645	7,068
Investing activities					
Capital expenditure	(5,386)	(5,511)	(4,966)	(6,659)	(7,231)
Others	(5,623)	1,184	1,667	(3,754)	(3,497)
Cash from Investing Activities	(11,009)	(4,327)	(3,299)	(10,414)	(10,728)
Financing activities					
Debt raised / (repaid)	4,238	325	6,363	5,119	2,906
Dividend paid	0	0	(1,354)	(1,225)	(1,207)
Others	(7,617)	2,872	(1,338)	233	191
Cash from Financing Activities	(3,379)	3,198	3,671	4,128	1,890
Net Changes in Cash	(3,672)	(8,655)	766	1,359	(1,770)
Adjustments	7,620	1,129	0	0	0
Cash at Beg of Year	36,970	40,917	33,391	34,158	35,517
Cash at End of Year	40,917	33,391	34,158	35,517	33,747

Financial Ratios					
	2016A	2017A	2018F	2019F	2020F
Gross margin(%)	19.0%	19.9%	17.2%	17.9%	18.2%
EBIT margin (%)	4.3%	2.7%	4.9%	5.1%	5.1%
EBITDA margin (%)	6.4%	5.5%	7.4%	7.5%	7.5%
Net margin (%)	2.7%	3.3%	3.1%	3.1%	3.1%
ROE (%)	5.4%	5.1%	5.5%	6.2%	6.7%
ROA (%)	1.3%	1.4%	1.5%	1.6%	1.6%
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Inventory turnover (day)	110.0	144.8	136.8	144.0	144.0
AR turnover (day)	173.4	210.9	198.0	180.0	172.8
AP turnover (day)	177.3	224.4	180.0	180.0	180.0
EV/EBITDA(x)	3.4	6.7	5.1	5.2	5.6
Quick ratio (x)	0.9	0.8	0.8	0.7	0.7
Current ratio (x)	1.3	1.3	1.3	1.3	1.3

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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