

West China Cement

Bloomberg: 2233 HK Equity | Reuters: 2233.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

8 Nov 2022

HOLD

Last Traded Price (7 Nov 2022): HK\$0.810 (HSI : 16,596)
Price Target 12-mth: HK\$0.85 (5% upside) (Prev HK\$1.10)

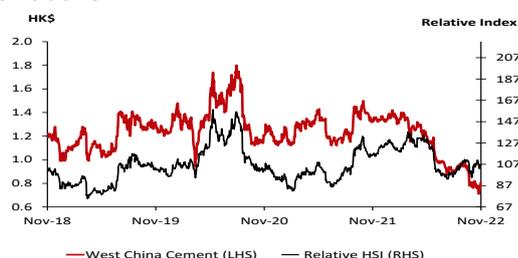
Analyst

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What's New

- 3Q22 earnings declined on GP contraction, in line
- Full inventory at warehouse preparing for longer off-peak production
- Overseas expansion on track; Conch's raising stake to limit of 30%
- Maintain HOLD and TP HK\$0.85

Price Relative



Forecasts and Valuation

FY Dec (RMBm)	2021A	2022F	2023F	2024F
Turnover	8,003	7,161	7,492	7,696
EBITDA	3,260	2,341	2,579	2,709
Pre-tax Profit	2,084	1,103	1,225	1,309
Net Profit	1,585	878	975	1,042
Net Profit Gth (Pre-ex) (%)	1.6	(44.6)	11.1	6.9
EPS (HK\$)	0.32	0.18	0.20	0.21
EPS Gth (%)	1.6	(44.6)	11.1	6.9
Diluted EPS (HK\$)	0.32	0.18	0.20	0.21
DPS (HK\$)	0.10	0.05	0.06	0.06
BV Per Share (HK\$)	2.27	2.39	2.53	2.68
PE (X)	2.5	4.6	4.1	3.9
P/Cash Flow (X)	2.1	1.5	1.6	1.6
P/Free CF (X)	nm	22.2	nm	6.8
EV/EBITDA (X)	1.7	2.4	2.4	2.2
Net Div Yield (%)	11.7	6.5	7.2	7.7
P/Book Value (X)	0.4	0.3	0.3	0.3
Net Debt/Equity (X)	0.1	0.1	0.1	0.1
ROAE (%)	14.6	7.6	7.9	8.0
Earnings Rev (%)		(28)	(33)	New
Consensus EPS (RMB)		0.26	0.29	0.33
Other Broker Recs:		B:2	S:1	H:1

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

Project restarts remain uncertain

Investment Thesis

Breaking into the overseas cement market. The company has invested in Africa since 2019, and this year, Mozambique produced 2mtpa, with Phase II of the construction about to kick off. The 1.5mtpa project in the Democratic Republic of the Congo is scheduled for production in the next two months, while the production of 1.5mtpa in Ethiopia (initial plan via a 61% stake acquisition) is expected to commence in Nov 23, representing one-fifth of the total sales mid-term.

Cement is a concentrated market in Shaanxi. West Cement (c.22mtpa in Shaanxi), Anhui Conch, Jidong, and Shengwei are the major producers in the province. West Cement is dominant in the southern Shaanxi market. Key infrastructure projects in railways, expressways, and hydraulic engineering are expected to drive cement demand from now to 2028, and West Cement is expected to benefit from the resumption of these projects.

Leveraging on strategic shareholder. Anhui Conch is the second largest shareholder with a board seat, supporting the company's sustained development.

Valuation:

Our TP of HK\$0.85 is based on 0.3x (prior 0.4x) FY23F P/B, pegged to its historical mean between 2018 and 2022.

Where we differ:

Our FY22F/FY23F earnings are below the consensus, to reflect the potential pressure on unit GP.

Key Risks to Our View:

Upside risk: Tighter market supply curb and environmental inspections and demand recovery exceeding expectations.

Downside risk: Weaker-than-expected pricing and GP.

At A Glance

Issued Capital (m shrs)	5,439
Mkt Cap (HKm/US\$m)	4,406 / 561
Major Shareholders (%)	
Zhang (Jimin)	32.3
Anhui Conch Cement Co Ltd	29.1
Free Float (%)	38.6
3m Avg. Daily Val. (US\$m)	0.94
GICS Industry: Materials / Construction Materials	

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WHAT'S NEW**3Q22 results hit by GP contraction; uncertainty from resumption of projects is an overhang**

3Q22 earnings decline largely in line. The company has reported its quarterly financial data for Yaobai Group in compliance with the bond market requirements. We note this represents the company's China operations but not its overseas business. 3Q22's revenue, GP and net earnings declined 5%, 10% and 28% y-o-y, respectively. The decline was mainly due to product margin decline and increased opex in the period. We believe these results are largely in line with expectations.

Shaanxi construction projects disrupted due to lockdowns.

Amid the Covid disruption on construction projects, the company's cement sales volume has been similar to the last quarter at approximately 4.5m tons. Unless those projects restart in mid-Nov, we believe the company would at best maintain its 2022 sales at last year's level. Meanwhile, management is also considering starting winter production suspension two weeks earlier (usually from Dec till Feb), which would translate to capacity utilisation dropping to c.60% and lower inventory level, which is now almost full at the warehouse.

Overseas development progress update. Recall the company has invested in Africa since 2019. The Mozambique project is set to produce 2mtpa this year, with 3Q22 sales at 500,000 tons, ASP US\$100 and GP US\$50, in line. The Phase II of the construction is about to kick off. The 1.5mtpa project in the Democratic Republic of the Congo is scheduled for production in the next two months, while the production of 1.5mtpa in Ethiopia (initial plan via a 61% stake acquisition) is expected to commence in Nov 23.

Conch buys up to limit of 30%. According to public information, Anhui Conch has brought its stake to 29.14% in West China Cement, and is the second largest shareholder after Mr. Zhang Jimin. This is close to the limit of 30% for a mandatory offer. Conch has appointed some representatives onto West Cement's board accordingly. Although we are not speculating on a potential offer, Anhui Conch's solid support should enable the company to better perform in strategic planning and development.

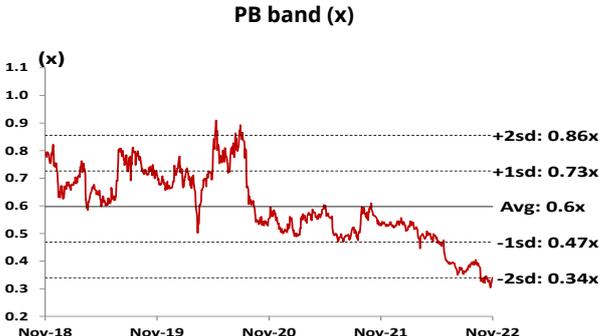
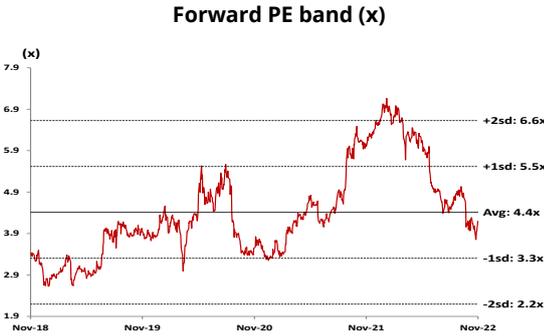
Maintain HOLD. We have slashed our FY22F/FY23F earnings by 28%/33% on lower GP assumptions. Although overall FY22F/FY23F earnings will return to 2017/2018's levels, we expect resumption of construction projects in Shaanxi and the company's overseas development to drive the rebound into 2023. Pegging at an unchanged 50% discount to Conch's valuation, we lower our target multiple to 0.3x FY23F P/B, suggesting limited downside to its current share price; and thus, we maintain HOLD rating.

Company Background

West China Cement is the largest cement producer in Shaanxi with a total cement capacity of 29.0mt p.a. (21.7mt p.a. in Shaanxi, 3.5mt p.a. in Xinjiang, 1.8mt p.a. in Guizhou, and 2.0mtpa in Mozambique) as at end-2021.

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Historical PE and PB band



Source: Thomson Reuters, DBS HK

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Key Assumptions

FY Dec	2020A	2021A	2022F	2023F	2024F
Sales volume for cement products (Mt)	19.9	20.3	19.4	20.4	20.4
ASP for cement products (RMB/t)	301.0	339.0	310.0	310.0	320.0
Gross profit for cement products (RMB/t)	100.0	105.0	55.0	60.0	65.0

Source: Company, DBS HK

Segmental Breakdown (RMB m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Revenues (RMB m)					
Cement	5,990	6,882	6,014	6,324	6,528
Aggregates	1,141	1,121	1,147	1,168	1,168
Total	7,131	8,003	7,161	7,492	7,696
Gross profit (RMB m)					
Cement	1,842	1,787	723	880	982
Aggregates	501	589	603	615	615
Total	2,342	2,377	1,325	1,494	1,596
Gross profit Margins (%)					
Cement	30.7	26.0	12.0	13.9	15.0
Aggregates	43.9	52.6	52.5	52.6	52.6
Total	32.8	29.7	18.5	19.9	20.7

Source: Company, DBS HK

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Income Statement (RMB m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Revenue	7,131	8,003	7,161	7,492	7,696
Cost of Goods Sold	(4,789)	(5,626)	(5,836)	(5,997)	(6,099)
Gross Profit	2,342	2,377	1,325	1,494	1,596
Other Opg (Exp)/Inc	(469)	(629)	(563)	(589)	(605)
Operating Profit	1,874	1,748	763	906	992
Other Non Opg (Exp)/Inc	(73)	426	200	200	200
Associates & JV Inc	17	2	0	0	0
Net Interest (Exp)/Inc	31	(92)	141	120	118
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	1,847	2,084	1,103	1,225	1,309
Tax	(264)	(301)	(159)	(177)	(189)
Minority Interest	(22)	(198)	(66)	(73)	(78)
Preference Dividend	0	0	0	0	0
Net Profit	1,560	1,585	878	975	1,042
Net Profit before Except.	1,560	1,585	878	975	1,042
EBITDA	2,719	3,260	2,341	2,579	2,709
Growth					
Revenue Gth (%)	(1.6)	12.2	(10.5)	4.6	2.7
EBITDA Gth (%)	(10.6)	19.9	(28.2)	10.1	5.1
Opg Profit Gth (%)	(6.4)	(6.7)	(56.4)	18.8	9.5
Net Profit Gth (%)	(13.4)	1.6	(44.6)	11.1	6.9
Margins & Ratio					
Gross Margins (%)	32.8	29.7	18.5	19.9	20.7
Opg Profit Margin (%)	26.3	21.8	10.6	12.1	12.9
Net Profit Margin (%)	21.9	19.8	12.3	13.0	13.5
ROAE (%)	16.1	14.6	7.6	7.9	8.0
ROA (%)	9.3	7.0	3.3	3.6	3.7
ROCE (%)	11.3	7.9	2.9	3.3	3.5
Div Payout Ratio (%)	41.9	29.9	29.9	29.9	29.9
Net Interest Cover (x)	NM	19.1	NM	NM	NM

Source: Company, DBS HK

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Balance Sheet (RMB m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Net Fixed Assets	11,161	13,885	15,006	16,033	16,516
Invt in Associates & JVs	78	0	0	0	0
Other LT Assets	2,497	3,928	3,928	3,928	3,928
Cash & ST Invt	1,375	4,222	4,141	3,805	4,091
Inventory	731	1,111	956	982	999
Debtors	3,064	3,502	2,893	3,026	3,109
Other Current Assets	0	0	0	0	0
Total Assets	18,906	26,648	26,924	27,775	28,643
ST Debt	1,879	3,250	3,250	3,250	3,250
Creditors	2,735	3,789	3,383	3,477	3,536
Other Current Liab	332	696	696	696	696
LT Debt	1,833	2,004	2,004	2,004	2,004
Other LT Liabilities	1,600	5,118	5,118	5,118	5,118
Shareholder's Equity	10,331	11,314	11,929	12,613	13,343
Minority Interests	196	478	544	618	696
Total Cap. & Liab.	18,906	26,648	26,924	27,775	28,643
Non-Cash Wkg. Capital	728	128	(231)	(164)	(124)
Net Cash/(Debt)	(2,337)	(1,032)	(1,112)	(1,449)	(1,162)
Debtors Turn (avg days)	33.9	33.9	33.9	33.9	33.9
Creditors Turn (avg days)	44.4	44.4	44.4	44.4	44.4
Inventory Turn (avg days)	34.4	34.4	34.4	34.4	34.4
Asset Turnover (x)	0.4	0.4	0.3	0.3	0.3
Current Ratio (x)	1.0	1.1	1.1	1.1	1.1
Quick Ratio (x)	0.9	1.0	1.0	0.9	1.0
Net Debt/Equity (X)	0.2	0.1	0.1	0.1	0.1
Net Debt/Equity ex MI (X)	0.2	0.1	0.1	0.1	0.1
Capex to Debt (%)	74.2	67.8	47.6	47.6	38.1
Z-Score (X)	2.1	2.3	2.3	2.3	NA

Source: Company, DBS HK

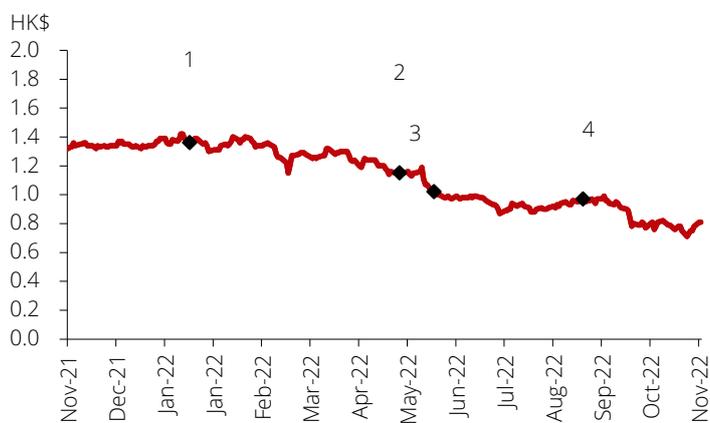
Cash Flow Statement (RMB m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Pre-Tax Profit	1,847	2,084	1,103	1,225	1,309
Dep. & Amort.	902	1,085	1,379	1,473	1,517
Tax Paid	(313)	(300)	(19)	(57)	(71)
Assoc. & JV Inc/(loss)	17	2	0	0	0
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	44	(914)	359	(66)	(40)
Other Operating CF	185	4	(141)	(120)	(118)
Net Operating CF	2,682	1,960	2,682	2,455	2,598
Capital Exp.(net)	(2,753)	(3,562)	(2,500)	(2,500)	(2,000)
Other Invt.(net)	23	64	0	0	0
Invt in Assoc. & JV	(288)	(232)	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(99)	214	0	0	0
Net Investing CF	(3,118)	(3,517)	(2,500)	(2,500)	(2,000)
Div Paid	(350)	(665)	(262)	(291)	(311)
Chg in Gross Debt	846	5,387	0	0	0
Capital Issues	0	0	0	0	0
Other Financing CF	(173)	(268)	0	0	0
Net Financing CF	322	4,453	(262)	(291)	(311)
Currency Adjustments	0	0	0	0	0
Chg in Cash	(114)	2,896	(81)	(336)	286
Opg CFPS (RMB)	0.48	0.53	0.43	0.46	0.48
Free CFPS (RMB)	(0.01)	(0.29)	0.03	(0.01)	0.11

Source: Company, DBS HK

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Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	17-Jan-22	HK\$1.39	HK\$1.60	Buy
2:	18-May-22	HK\$1.16	HK\$1.47	Buy
3:	7-Jun-22	HK\$1.02	HK\$1.10	Hold
4:	1-Sep-22	HK\$0.970	HK\$1.10	Hold

Source: DBS HK

Analyst: Duncan Chan

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DBS HK recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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