

January 29, 2013

Buy
Unchanged

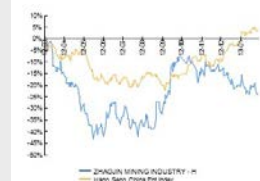
Attractive Valuation, Buy on dips

ZHAOJIN MINING INDUSTRY - H (1818 HK)

Market Data: Nov,15

Closing Price (HK\$)	11.56
Price Target (HK\$)	15.02
HSCEI	12,100
HSCCI	4,656
52-week High/Low (HK\$)	16.06/8.00
Market Cap (USD Mn)	4,343
Market Cap (HK\$ Mn)	33,696
Shares Outstanding (Mn)	874
Exchange Rate (RMB-HK\$)	1.23

Price Performance Chart:



Source: Bloomberg

Analyst

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Related Reports

"Zhaojin Mining- Gold sales speed up in 3Q, upgrade to BUY" Oct 30, 2012

"Sales volume decreased, interim result below expectation" Aug 20, 2012

"Gold price correction provides attractive entry point" June 26, 2012

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Financial summary and valuation

	2010	2011	2012E	2013E	2014E
Revenue (RMB million)	4,098	5,741	7,098	7,758	8,868
YOY (%)	46.51	40.10	23.63%	9.29%	14.32%
Net income (RMB million)	1,202	1,662	1,758	1,978	2,512
YOY (%)	59.38	38.27	5.81	12.49	27.00
EPS (RMB)	0.28	0.57	0.60	0.68	0.86
Diluted EPS (RMB)	0.28	0.57	0.60	0.68	0.86
ROE (%)	21.51	24.62	22.46	21.06	21.91
Debt/asset (%)	39.81	49.65	37.31	33.36	31.40
Dividend Yield (%)	2.13	1.84	1.82	1.87	2.24
P/E (x)	19.72	14.27	15.58	13.85	10.91
P/B (x)	4.10	4.43	3.28	2.73	2.24
EV/EBITDA (x)	15.48	11.68	9.31	7.45	5.92

Note: Diluted EPS is calculated as if all outstanding convertible securities, such as convertible preferred shares, convertible debentures, stock options and warrants, were exercised. P/E is calculated as closing price divided by each year's EPS.

Investment Highlights:

- We believe gold's super cycle has not turned yet. US debt ceiling problem will be the next catalyst for gold price to rally. In Aug 2011, market started to worry about the US long term debt as debt ceiling problem hit deadline. Gold price increased a lot upon this event. We believe similar thing might happen in near term and gold price will eventually go up.
- Last Friday, The Fed's weekly update showed that total assets hit USD 3 trillion on Jan 23 2013, a historical high. As we previously discussed in our December Gold Theme report, we believe there is a significantly positive correlation between the size of Fed's balance sheet and the gold price. The Fed balance sheet did not immediately expand significantly after QE3 possibly due to the time taken for the Fed to make MBS transactions. Now it is expanding at a fast pace and we believe the trend will also continue, provide strong catalyst for gold price to go up.
- Recent share price correction provides attractive entry point. We have compared the historical valuations of Zhaojin and Zijin and find that the current valuation gap between Zhaojin and Zijin is at a two-year low. We therefore see significant upside for Zhaojin Mining if the gold price rises.
- Zhaojin is our top pick in this sector. We believe the company will continue to deliver high growth in terms of own-mined gold production. We raise our earnings forecast for 2013 to reflect better cost control, higher sales and production volume. We also adjust down our assumption for the gold price in 2014 from USD 2,000 to 1,850 and therefore revise down our 2014 earnings forecast. This leaves our 2012/13/14 EPS forecasts at 0.60/0.68/0.86 (prev: 0.60/0.65/0.99). The company is trading at 15x 12E P/E and 14x 13E P/E. Our new target price of \$15.02 (prev: \$15.90) represents 18x 13E P/E. We maintain our Buy rating and recommend buying on dips.

投资要点：

- 我们认为黄金的超级周期尚未结束。美国债务上限问题将会成为黄金下一个重要催化剂。2011年八月，债务上限问题就曾引起市场对美国长期债务违约的担忧，促使黄金价格在那段时间快速上涨。我们认为类似的情况很有可能再发生。
- 上周五，美联储公布最新的资产负债表情况。总资产于2013年1月23日当日超过3万亿美元，创下历史新高。在我们之前十二月的黄金主题报告中，我们讨论了美联储资产负债表与金价的关系。我们发现两者正相关性极强。9月QE3后，资产负债表并未明显扩张，引起了市场担忧，我们认为这主要由于MBS的交割时间比较长。现在美联储资产负债表加速扩张，我们相信该趋势会持续，并带动金价上涨。
- 近期招金矿业股价调整很多，提供了买入机会。我们比较了招金矿业(1818.HK)和紫金矿业(2899.HK)的历史估值价差，发现目前的估值差位相对的历史低位，我们相信随着黄金的上涨，招金股价的上行空间很大。
- 公司为我们行业内首选。我们相信未来公司矿产金能继续高速增长。我们提高了公司2013年的盈利预测，为了体现公司更好的成本控制，和产量增长。我们同时下调了2014年的黄金均价至1850美元/盎司(之前为2000美元/盎司)，从而下调2014年EPS。我们预测公司12/13/14年EPS为0.60/0.68/0.86(之前为0.60/0.65/0.99)。公司目前市盈率为12年15倍，13年14倍。基于18倍的13年市盈率，我们给予公司15.09港币的新目标价(之前为15.9港币)。我们维持公司买入评级，推荐逢低买入。

Investment Case

Valuation and Target Price

We maintain our BUY rating on this stock and adjust our target price to HKD 15.02

Key Assumptions

We adjust our assumption that gold price will averages at USD 1800/1850 per oz for year 2013/2014.

How we differ from consensus

- 1) Market has concerned if gold's super cycle has ended. We believe the turning point has not come yet. Gold price fell after QE3 and has fluctuated at the current level for a while. The latest Fed minutes showed that Fed might exit QE before the end of 2013, which put strong downward pressure on gold price. Many investors are now worrying if the long run upward trend for go has ended. However, we don't think gold price will turn around in short term. The US are still facing fiscal cliff and more recently they will face the problem of debt ceiling. This can be a catalyst for gold price to go up if debt ceiling problem becomes serious.
- 2) In the HK market, comparisons between Zhaojin's and Zijin's historical P/E ratios provide meaningful indications. Using data since Oct 2009, we have divided Zhaojin's share price by Zijin's share price to get a valuation gap ratio that reflects the valuation movement difference between the two stocks. The average ratio is 1.69x meaning Zhaojin's P/E valuation is 1.69x that of Zijin on average within the period. The recent downward share price correction has made Zhaojin now very attractive compared to Zijin. The current ratio of 1.45x is near the previously too-low level and we believe the gap will bottom out. We still believe there is significant upside potential for Zhaojin if the gold price continue to be strong.

Catalysts

- 1) Fed's Balance Sheet continues to expand in a fast pace
- 2) Market starts to worry about the US's long term debt as debt ceiling limit is reaching.

Risks to central scenario

The major risk also falls in gold price. We believe a faster US economic recovery will put strong pressure on gold price.

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Summary

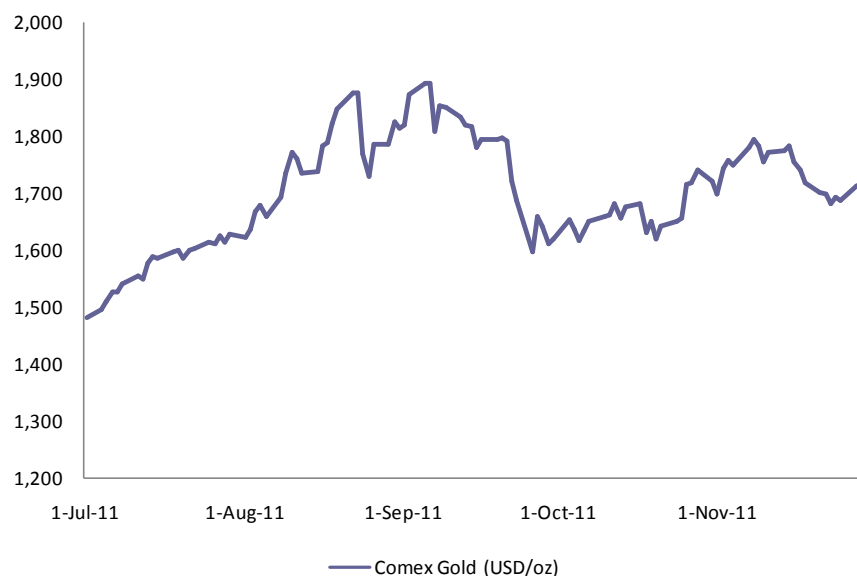
We believe Zhaojin's recent price correction provides an attractive entry point given our positive view on the gold price. We do not believe gold's super cycle has turned yet, we expect the US debt ceiling issue to become a major catalyst for a rally in the gold price, and believe the Fed's balance sheet expansion will continue, even after hitting a record high.

Gold: Super cycle has not turned yet, focus on US debt ceiling 2.0

The gold price fell following the implementation of QE3 and has fluctuated at current levels for some time. The latest Fed minutes indicate that it might exit QE before the end of 2013, something which has put strong downward pressure on the gold price. This has led to concern among investors that the upward trend in the gold price has come to an end. However, we do not expect a turnaround in the gold price in the short term. The US is still facing issues related to the fiscal cliff, but will first come up against debt-ceiling related issues, something which could be an upside catalyst for the gold price if it becomes more serious.

The debt ceiling became a problem for the US back in July/Aug 2011, leading to market concern about long-term US debt. Despite the debt ceiling bill of Aug 2 2011, Standard & Poor's still downgraded US debt, further stoking concern. There was a strong rise in the gold price during this period.

Fig 1: Gold Price performed very well during 2011 US debt ceiling (USD/oz)

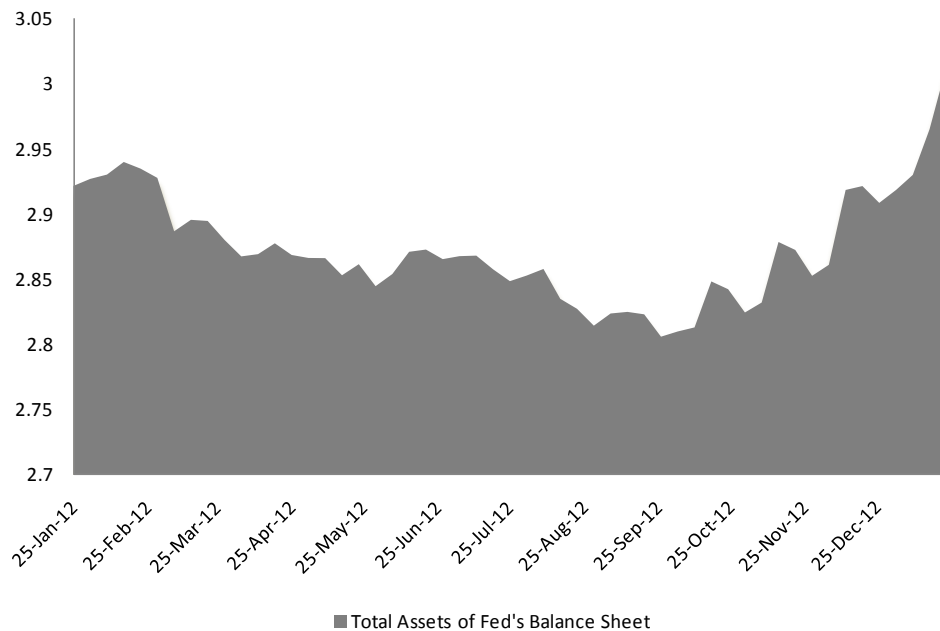


Source: Company data, SWS Research

Fed Balance Sheet has begun to expand quickly

As we previously expected, The Fed's balance sheet has been expanding quickly since January. Last Friday, The Fed's weekly update showed that total assets hit USD 3 trillion on Jan 23 2013, a historical high. As we previously discussed in our December Gold Theme report, we believe there is a significantly positive correlation between the size of Fed's balance sheet and the gold price. The Fed balance sheet did not immediately expand significantly after QE3 possibly due to the time taken for the Fed to make MBS transactions.

Fig 2: Fed Balance Sheet hit 3 trillion last week (USD trillion)

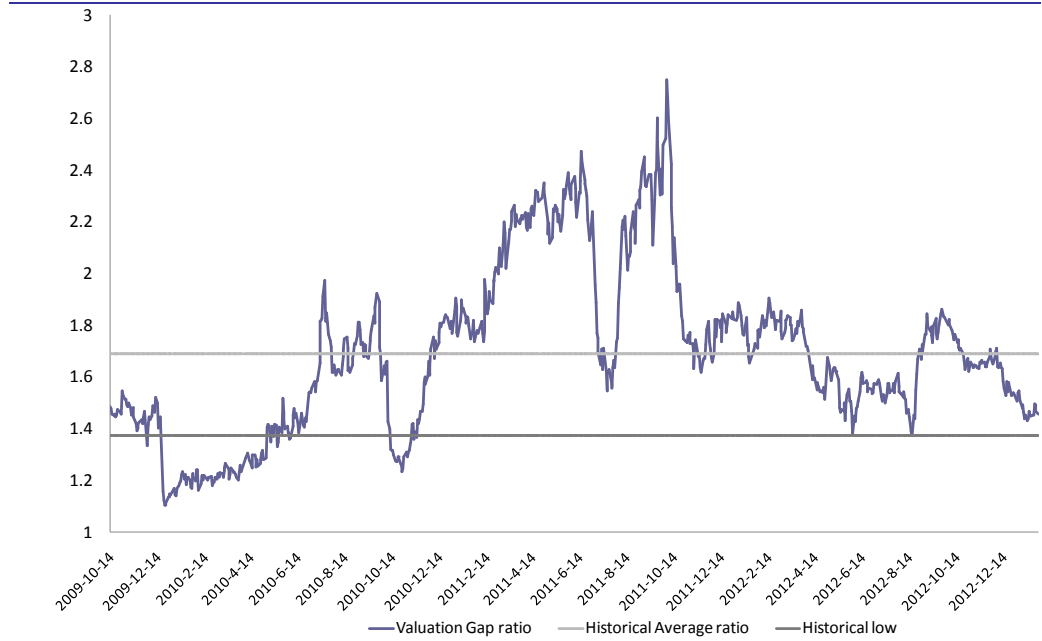


Source: Fed, SWS Research

Valuation gap suggests its right time to BUY

In the HK market, comparisons between Zhaojin's and Zijin's historical P/E ratios provides meaningful indications. Using data since Oct 2009, we have divided Zhaojin's share price by Zijin's share price to get a valuation gap ratio that reflects the valuation movement difference between the two stocks. The average ratio is 1.69x meaning Zhaojin's P/E valuation is 1.69x that of Zijin on average within the period. The recent downward share price correction has made Zhaojin now very attractive compared to Zijin. The current ratio of 1.65x is near the previously too-low level and we believe the gap will bottom out. We still believe there is significant upside potential for Zhaojin if the gold price continue to be strong.

Fig 3: Zhaojin-Zijin valuation gap ratio shows attractive buy point



Source: Bloomberg, SWS Research

Appendix

Consolidated Income Statement

million yuan	2009	2010	2011E	2012E	2013E	2014E
Revenue	2,797	4,098	5,741	7,098	7,758	8,868
Cost of Sales	(1,348)	(1,787)	(2,677)	(3,455)	(3,547)	(3,990)
Gross Profit	1,449	2,311	3,064	3,643	4,210	4,878
Other Income	25	1	(9)	(20)	0	0
Distribution expenses	(38)	(38)	(56)	(50)	(62)	(89)
Administrative expenses	(382)	(547)	(615)	(923)	(1,008)	(1,242)
EBITDA	1,263	2,110	2,874	3,070	3,660	4,173
EBIT	1,029	1,726	2,393	2,670	3,140	3,548
Finance income and expenses	(10)	(75)	(98)	(245)	(253)	(102)
Profit before tax	1,054	1,727	2,246	2,650	3,044	3,635
Income tax expense	(264)	(410)	(564)	(550)	(698)	(883)
Minority interests	(3)	40	61	97	115	138
Profit for the year	754	1,202	1,662	1,758	1,978	2,512

Consolidated Cash Flow Statement

million yuan	2009	2010	2011	2012E	2013E	2014E
Profit before taxation	1,015	1,652	2,287	2,405	2,791	3,533
Plus: Depr. and amortisation	234	384	480	400	521	625
Finance cost	23	92	98	250	260	115
Losses from investments	(26)	23	44	0	0	0
Change in working capital	13	(689)	(340)	(131)	(54)	(171)
Others	26	(21)	(4)	(1)	(3)	(8)
Tax paid	(332)	(357)	(446)	(550)	(698)	(883)
CF from operating activities	952	1,084	2,079	2,373	2,817	3,211
CAPEX	(963)	(1,914)	(1,898)	(600)	(600)	(600)
Other CF from investing activities	140	41	(371)	5	7	17
CF from investing activities	(823)	(1,873)	(2,270)	(595)	(593)	(583)
Equity financing	0	0	0	0	0	0
Net change in liabilities	1,658	(241)	1,224	(1,010)	0	0
Dividend and interest paid	(261)	(406)	(582)	(748)	(773)	(730)
Other CF from financing activities	0	8	12	0	0	0
CF from financing activities	1,397	(639)	654	(1,759)	(773)	(730)
Net cash flow	1,526	(1,428)	463	19	1,452	1,897
FCFF	49	(903)	71	1,789	2,309	2,519
FCFE	1,684	(1,237)	1,197	529	2,049	2,403

Consolidated Balance Sheet

million yuan	2009	2010	2011E	2012E	2013E	2014E
Current Assets	3,018	2,183	3,970	3,410	4,976	7,208
Bank balances and cash	2,209	782	1,246	1,263	2,715	4,612
Trade and other receivables	207	572	567	631	705	847
Inventories	475	779	2,139	1,507	1,547	1,740
Other current assets	126	49	18	9	9	9
Long-term investment	45	46	67	70	72	72
PP&E	2,763	3,691	4,926	5,272	5,497	5,018

Intangible and other assets	2,756	3,494	4,336	3,586	3,448	3,121
Total Assets	8,582	9,415	13,298	12,338	13,994	15,419
Current Liabilities	1,551	1,485	3,918	2,245	2,315	2,538
Borrowings	611	370	1,510	500	500	500
Trade and other payables	823	847	1,941	1,242	1,302	1,466
Other current liabilities	117	268	467	503	513	572
Long-term liabilities	2,063	2,154	2,375	1,748	1,637	667
Total Liabilities	3,614	3,639	6,293	3,993	3,953	3,205
Minority Interests	400	388	414	608	839	1,114
Shareholder Equity	4,567	5,387	6,592	7,738	9,203	11,100
Share Capital	1,457	1,457	2,915	2,915	2,915	2,915
Reserves	1,788	1,833	1,216	1,216	1,216	1,216
Retained earnings	1,322	2,097	2,460	3,606	5,071	6,968
Total Liabilities and equity	8,582	9,415	13,298	12,338	13,994	15,419

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Rong Ye: Equity Analyst

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Buy : with a markup more than 20% better than that of the market ;

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Neutral : with a markup less than 5% better or worse than that of the market ;

Underperform : with a markup more than 5% worse than that of the market.

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Neutral : Industry performs about the same as that of the whole market ;

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