

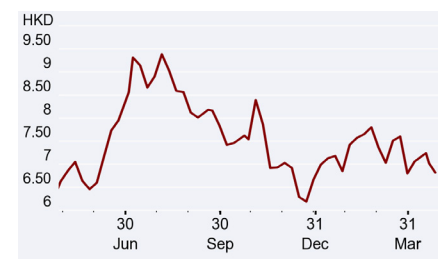
Zhaojin Mining Industry (1818.HK)

Results: 1Q17 Result Inline but Missed Consensus; Possible Short Term Headwinds

- Citi's Take** — Zhaojin reported PRC GAAP 1Q17 net profit of Rmb120mn (0.04/share), vs. Rmb14mn net profit in 1Q16. The result is inline with our estimate at Rmb126mn. It represents 21% of our full year estimate and 18% of consensus. Included in 1Q17 net profit, was Rmb60mn non-core earnings mainly from fair value and investment gains. Excluding these one-offs for 1Q17 and 1Q16, net profit more than doubled YoY to Rmb78mn in 1Q17.
- Margin expansion not seen despite gold price increase** — Shanghai gold price up 11%YoY to Rmb273/g during the quarter. While company's gross margin remain flattish YoY at 37%. This might be due to cost increase or more revenue from less profitable tolling or buyout of gold business.
- Finance cost increased 31%YoY, due to steadily increasing net gearing** — The ratio increased from 64% at June 2016 to 76% at Dec 2016 and further to 80% at Mar 17.
- Implications — Slight negative:** 1Q17 result is inline with Citi estimate but missed consensus. However, we don't expect market to react strongly towards the result because it lacks meaningful operating data. The most important driver for company's share price is still gold price, with correlation of 0.92 in the past five years. Citi's latest gold price forecast is US\$1,220/oz for 2017e. Citi sees prices supported around a \$1,200-handle for most of 2017, despite a more hawkish than consensus Fed outlook and moderately bullish USD outlook for 2H. Trump policy risks, geopolitical uncertainty and the potential for further inflation surprises all seem more supportive for gold sector investment versus the initial 'Trumpflation' market reaction of 4Q'16.

Buy/High Risk	1H
Price (28 Apr 17 16:10)	HK\$6.76
Target price	HK\$9.20
Expected share price return	36.1%
Expected dividend yield	0.6%
Expected total return	36.7%
Market Cap	HK\$21,772M
	US\$2,798M

Price Performance (RIC: 1818.HK, BB: 1818 HK)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Dec	(RmbM)	(Rmb)	(%)	(x)	(x)	(%)	(%)
2015A	308	0.104	-32.3	57.7	1.7	3.2	0.7
2016A	353	0.118	13.8	50.7	1.6	3.2	0.7
2017E	571	0.191	61.5	31.4	1.5	5.0	1.1
2018E	645	0.216	13.1	27.8	1.5	5.4	1.2
2019E	863	0.289	33.7	20.8	1.4	6.9	1.6

Source: Powered by dataCentral

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Figure 1. Quarterly result snapshot

Key operating data	1Q15	2Q15	3Q15	4Q15	1Q16	2Q16	3Q16	4Q16	1Q17	Citi Est	Diff	YoY	QoQ
Gold price (Rmb/g)	247	238	229	230	246	263	287	272	273	271	1%	11%	0%
Key financial data													
Revenue	1,033	1,688	1,449	1,717	1,283	1,979	1,545	1,892	1,489	1,463	2%	16%	-21%
Gross profit	503	627	610	491	483	922	547	736	547	585	-7%	13%	-26%
SG&A	(244)	(307)	(302)	(203)	(286)	(191)	(356)	(229)	(261)	(241)	8%	-9%	14%
EBIT	261	362	261	157	169	370	455	126	345	305	13%	104%	174%
Finance costs	(107)	(195)	(79)	(104)	(104)	6	(296)	64	(137)	(76)	80%	-31%	-313%
Income tax	(39)	(60)	(71)	15	(25)	(148)	(8)	(184)	(55)	(80)	-31%	118%	70%
Net profit	97	97	93	22	14	233	87	(14)	120	126	-5%	737%	949%
EPS	0.03	0.03	0.03	0.01	0.005	0.08	0.03	(0.00)	0.04	0.04	-5%	737%	949%
Margins													
Gross profit	49%	37%	42%	29%	38%	47%	35%	39%	37%	40%	-3.3ppt	-0.9ppt	-2.2ppt
EBIT margin	25%	21%	18%	9%	13%	19%	29%	7%	23%	21%	2.3ppt	10.0ppt	16.5ppt
Net margin	9%	6%	6%	1%	1%	12%	6%	-1%	8%	10%	-2.1ppt	6.9ppt	8.8ppt
SG&A % of revenue	24%	18%	21%	12%	22%	10%	23%	12%	18%	16%	1.1ppt	-4.8ppt	5.5ppt
Effective tax rate	29%	38%	43%	-218%	64%	39%	8%	108%	31%	39%	-7.3ppt	-32.4ppt	-76.8ppt
ROE	4%	4%	3%	1%	0%	9%	3%	-1%	4%	NA	NA	3.8ppt	4.8ppt
Net gearing	80%	81%	70%	61%	69%	64%	66%	76%	80%	NA	NA	11.4ppt	3.9ppt
FCF	(142)	(494)	193	(30)	(178)	564	(362)	617	120	NA	NA	-167%	-81%

Source: Company Data, Citi Research

Zhaojin Mining Industry

Valuation

We value Zhaojin at HK\$9.20/sh, based on the average of DCF and PB valuations. Under our DCF valuation, we assume a long-term gold price of US\$1,370/oz, in line with our commodity team's forecast. With a 3% terminal growth and a WACC of 6%, our NPV/share works out to HK\$9.27/sh. In our PB valuation, which derives a fair value of HK\$9.05/sh, we assign 2.0x 17E PB, which is set below the historical mean of 2.5x since 2011 to reflect our view that future ROE will be below that of peers and also below the company's historical levels.

Risks

Our quantitative model assigns a High Risk rating to Zhaojin based on the volatility of its share-price movements in the past 12 months. Major downside risks that could mean the shares fail to achieve our target price include: 1) gold prices are lower than we expect due to a spike in interest rates; 2) production costs are higher than we are modelling; 3) capex outlays overrun at the Haiyu Gold mine and/or there are production delays.

Appendix A-1

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Zhaojin Mining Industry (1818.HK)

Ratings and Target Price History Fundamental Research

Analyst: Ada Gao, CFA
Covered since December 5 2016



	Date	Rating	Target Price	Closing Price
1	11-Feb-15 05:40:19	*3	*4.10	4.65
2	01-Jun-15 17:46:14	*2	*6.70	5.95
3	14-Oct-15 18:21:51	2	*5.10	4.65

	Date	Rating	Target Price	Closing Price
4	11-Dec-15 06:01:07	2	*4.50	4.04
5	02-May-16 13:38:49	2	*6.80	6.63
6	15-Jul-16 01:11:35	Coverage terminated		

	Date	Rating	Target Price	Closing Price
7	05-Dec-16 00:12:34	*1H	*9.20	6.85

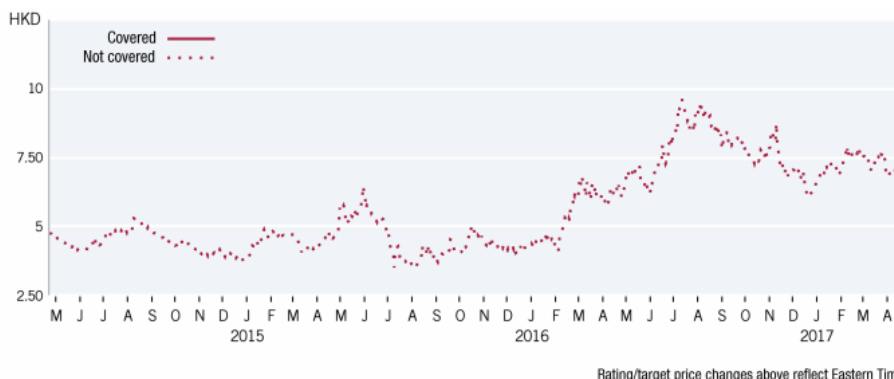
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Rating/target price changes above reflect Eastern Time

Zhaojin Mining Industry (1818.HK)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ada Gao, CFA
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Data current as of 31 Mar 2017

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	64%	63%	61%	61%	64%	47%

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