

Chinavtm Mining (00893.HK/893 HK)

Titanium price rebound to boost 2012 results

HK\$1.64

Outperform

Initial coverage

Company visit

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- Regional price fluctuations milder; 12-year iron ore earnings up a marginal 4.3%
- Vietnam to impose export ban in 2012; the company's high-grade titanium concentrate sales ratio expected to rise from 9.7% in 2011 to 15.2% in 2012
- We forecast 2011 & 2012 EPS of HK\$0.34 & HK\$0.38, respectively; initiate coverage with Outperform rating

Largest private iron ore supplier in Sichuan

As the biggest private iron ore supplier in Sichuan, the company engages in mining and washing of vanadium-titanium magnetite, as well as producing and selling of pellets and titanium concentrate. Primary customers are steel makers in Sichuan, Yunnan and downstream users of titanium.

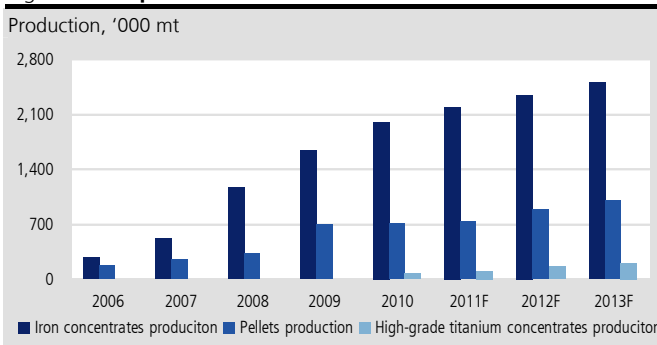
The company owns seven mines, of which four are in operation, two are under construction, and one is under exploration. The company owns five iron ore washing plants. The company's Baicao Mine, Xiushuihe Mine, Yangquejin Mine and Cizhuqing Mine are all open-pit mines, supplying vanadium-titanium magnetite. Iron accounts for 25-30% while titanium accounts for 10-11%. The mines' ferrovanadium output capacity stands at 27mn metric tons (mt). The company owns Maoling Mine and Yanglongshan Mine in Wenchuan region. Resources there are mainly ordinary magnetite. Output capacity of iron concentrates is 150k mt. Currently, the company has 336mn mt of iron ore. Known reserves are 144mn mt, which is enough to supply the company's operations for the next 20 years.

Mine expansion on hold; growth of iron output lacklustre

A 400-meter separation zone exists between Yangque Mine and Xiushuihe Mine. It is estimated that 70mn mt of reserves exist there. Mine expansion planning is due to be completed in end-2012. Yanglongshan Mine in Wenchuan is still in the exploration phase. Production won't begin until 2014. Yanyuna Mine, in which the company has a 51% stake, is also in exploration phase. Mining permit application and mine expansion will be finished some time after 2013. The company produced 1.04mn mt of iron concentrate in 1H11, while as much as 2mn mt of iron concentrate had been produced as of end-November. Full-production is estimated to be 2.2mn mt. Maoling Mine in Wenchuan is undergoing pilot production and therefore can only produce 27mn mt ordinary iron concentrates in 1H11. Full-year production at Maoling Mine is forecast to be 30,000 mt. Judging from the company's current mine expansion plans, iron concentrates output in 2012 is expected to hit 2.35mn mt, up 6.8% YoY. Output growth momentum is less than satisfactory.

New pellet plants began production in May, totalling 1.36mn mt of output capacity. As around 30% of the company's iron concentrates output is used in processing pellets, and given that iron concentrate also needs to be processed, margin contribution is limited. The company produced 300,000 mt of pellets in 1H11. Full-year production is expected to reach 700,000 mt. The company plans to produce 880,000 mt of pellet in 2012, up 20% YoY.

Figure 1: Output estimates in 2011-13



Source: Company data; KGI Asia Limited

Regional price fluctuations milder; 12-year iron ore earnings up slightly

As Sichuan and Yunnan are inland provinces, iron ore transportation is somewhat inconvenient. As such, regional iron concentrate markets mainly supply local customers. Some supply is from imports. The ASP of vanadium-containing iron powder, released by the company, reached a low of Rmb558/mt in 2008, while in 2009 it was Rmb665/mt. Prices fluctuations in Tangshan, China's major steel-producing region, were far greater than those in the Southwest. Tangshan's iron concentrate ASP in 2008 (wet basis, tax excluded) was Rmb1036/mt. ASP in 2009 was Rmb593/mt, dropping by 43%. 4Q12 imported iron concentrate price declined from US\$195/mt to US\$155/mt. Vanadium iron price in Panxi declined from Rmb650/mt in 3Q11 to Rmb580/mt, down by around 11%. Compared with the huge price fluctuations across iron concentrate in the east, the company's Vanadium iron concentrate price is relatively stable, stabilizing the company's earnings.

Figure 2: Iron prices in Hebei Tangshan down slightly

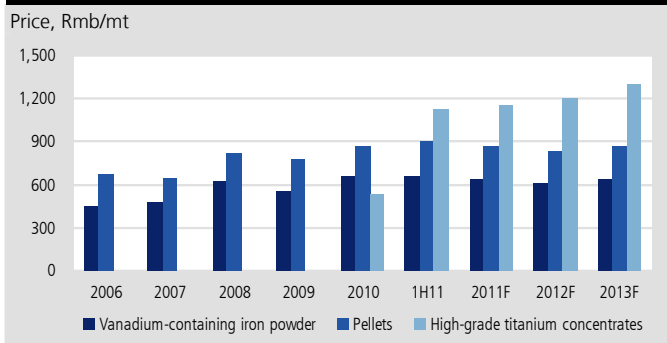


Source: Company data; KGI Asia Limited

The ASP of vanadium iron powder in 1H11 was Rmb664/mt, for a gross margin of around 58%. Vanadium iron powder price in Panxi has dropped to Rmb580-590/mt, while gross margin has declined to

around 52%. We expect ASP on vanadium iron powder in 2011 and 2012 to be Rmb640/mt and Rmb610/mt, respectively. Iron concentrates sales in 2012 displayed slight growth. The company's iron ore business yielded gross profit of Rmb800mn in 2012, up by around 4.3% YoY. The firm's core business profits maintained moderate growth.

Figure 3: Company's price estimates on major products in 2011-20



Source: Company data; KGI Asia Limited

Vietnam imposes export ban; high-grade titanium concentrate the expansion catalyst for 2012

High-grade titanium concentrate price hovered at Rmb500-600 in 2006-2010, before declining slightly during the 2009 financial crisis. Titanium concentrate price began to rebound in 2010, rising to Rmb1,000/mt by year end. Titanium concentrate price has seen even more dramatic gains in 2011. On June 22, Vietnam announced that titanium concentrate exports would likely terminate at end-2011, prompting high-grade titanium concentrate price to rise to Rmb2,300/mt in mid-June. Currently, high-grade titanium concentrate price has fallen back to Rmb1,000/mt. In 2010, China imported 2.04mn mt of titanium concentrate, of which 40% was from Vietnam. Given China's relatively high reliance on Vietnam titanium imports, if Vietnam terminated, or even cut, titanium exports to China in 2012, China's titanium price would gradually rise to high levels.

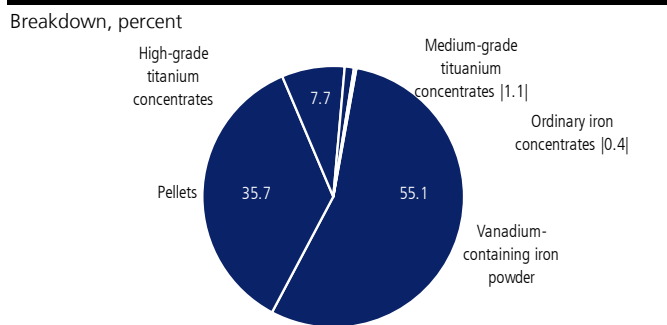
The company sold 61.7mn mt of high-grade titanium concentrate in 2010. Realized sales in 2011 are expected to hit 110k mt. With significant titanium concentrate price gains, 2010 titanium concentrate sales ratio has risen quickly to 8.8%. According to the company's 2011 mid-year report, the company's high-grade titanium concentrate production costs were about Rmb400, with gross margin nearing 65%. High-grade titanium concentrates price in Sichuan has risen from a low of Rmb1200/mt to Rmb1500/mt. High-grade titanium concentrates price is expected remain high in 2012. Gross margin is expected to stay above 65%. We estimate the company's high-grade titanium concentrate sales to reach 180k mt in 2012, contributing Rmb145mn in gross profit (up 75% YoY), and adding Rmb0.02-0.03 to EPS.

We forecast 2011 & 2012 net profits to grow 10.1% & 11.7%

The company's iron concentrate production in 2012 is expected to grow a little more. Pellet production growth is estimated to reach 20%, though contribution to gross margin will be limited. In 2012, high-grade titanium concentrate production is expected to see a substantial increase at 60%, providing key profit growth

momentum. We anticipate the company's 2011 and 2012 sales at Rmb1.71bn and Rmb1.92bn, up 10.0% and 12.1%, respectively. Net profits are forecast to hit Rmb587mn and Rmb656mn, up 10.1% and 11.7%, respectively. EPS is estimated to come in at HK\$0.34 and HK\$0.38.

Figure 4: Chinavtm Mining's 1H11 profit structure



Source: Company releases; KGI Asia Limited

Valuation and Recommendation

The company's 2012 iron concentrate production is expected to remain stable. Profit contribution of iron ore business is expected to display slight growth. As Vietnam will likely impose an export ban on titanium concentrate in 2012, China's high-grade titanium concentrate price has likely bottomed out. 2012 prices will likely remain at high levels. If Vietnam terminated titanium concentrate exports, China's high-grade titanium concentrate price would come in higher than expected. Meanwhile, the company's high-grade titanium concentrate production is set to skyrocket 60%. The decent profitability of high-grade titanium concentrate is expected to be the company's key growth driver for 2012. We forecast 2011, 2012 and 2013 EPS at Rmb0.28, Rmb0.32 and Rmb0.33, respectively. We derive a 6-month target price of HK\$2.04, 6x our 2011 PE, implying 24.4% upside compared with the current price HK\$1.64. We initiate coverage with our Outperform rating.

Figure 5: Peer comparison

Company	Ticker	FCY	Market cap US\$m	Rating	Price	Currency	Target price (HK\$)	EPS		P/E(x)		BVPs P/B(x)	
								2011F	2012F	2011F	2012F	2011F	2011F
Chinavtm Mining	00893.HK	RMB	431.0	Outperform	1.64	HK\$	2.04	0.34	0.37	4.9	4.4	1.57	1.0
CMOC	03993.HK	RMB	2,425.6	Neutral	3.81	HK\$	3.60	0.31	0.34	12.2	11.3	2.49	1.5
Zhaojin Mining	01818.HK	RMB	5,231.8	Neutral	14.12	HK\$	17.00	0.70	0.76	20.3	18.7	2.66	5.3
China Hanking	03788.HK	RMB	656.9	Not Rated	2.60	HK\$	NA	NA	NA	NA	NA	NA	NA
Xinxin Mining	03833.HK	RMB	677.2	Not Rated	2.43	HK\$	NA	0.21	0.31	11.4	7.8	2.63	0.9
CITIC Dameng	01091.HK	HK\$	465.4	Not Rated	1.23	HK\$	NA	0.16	0.24	7.5	5.2	1.31	0.9
Minmetals Resources	01208.HK	RMB	2,298.9	Not Rated	3.43	HK\$	NA	0.14	0.10	25.0	33.3	0.33	10.5
Zijin Mining Group	02899.HK	RMB	13,307.3	Not Rated	3.54	HK\$	NA	0.30	0.36	11.9	9.8	1.29	2.7
Average										13.6	13.4		3.4

Source : KGI Asia Limited

Figure 6: Chinavtm Mining's 12-month forward PE band



Source : KGI Asia Limited estimates

Year to 31-Dec	Sales (Rmb mn)	Gross profits (Rmb mn)	EBIT (Rmb mn)	EBITDA (Rmb mn)	Net profits (Rmb mn)	EPS (Rmb)
2010A	1,554	830	689	761	533	0.26
2011F	1,710	853	696	813	587	0.28
2012F	1,917	949	784	930	656	0.32
2013F	2,182	1,074	902	1,065	680	0.33
Year to 31-Dec	EV/Sales (x)	EV/EBIT (x)	EV/EBITDA (x)	P/E (x)	EV/Inv. C. (x)	ROAE (%)
2010A	4.5	10.1	9.2	15.5	2.3	20.2
2011F	1.6	4.0	3.5	6.1	0.7	19.1
2012F	1.3	3.1	2.6	5.5	0.5	17.8
2013F	0.9	2.3	1.9	5.3	0.4	15.6
Sector		Metal	52-week trading range (HK\$)			1 - 3.9
12M target price (HK\$/shr)		2.04	Mkt cap-HK\$ bn/US\$ mn			3.4/436
Upside/downside (%)		24.4	Outstanding shares (mn)			2,075
The percentile of excess return (%)		56	Free floating shares (%)			42
Dividend yield-12/11E (%)		N.A.	The Largest Shareholder (%): Mr.Wang Jin			58
Book value/shr-12/11E (Rmb)		1.6	3M avg. daily trading (mn)			9
P/B-12/11E (x)		1.1	Abs. Performance (3,6,12M)(%)			-21.9; -39; -55.8
Net debt/equity-12/11 (%)		Cash	Rel. Performance (3,6,12M)(%)			-21.8; -27.5; -46

Balance Sheet

Year to 31 Dec (Rmb mn)	2009A	2010A	2011F	2012F	2013F
Total Assets	3,073	3,733	4,477	5,268	6,086
Current Assets	2,233	1,473	1,754	2,285	2,736
Cash & ST Investments	1,884	1,096	1,320	1,779	2,209
Inventories	71	70	83	98	110
Accounts Receivable	187	208	244	289	281
Others	91	100	107	120	136
Non-current Assets	840	2,261	2,723	2,982	3,351
LT Investments	0	0	0	0	0
Net fixed Assets	496	1,476	1,736	1,848	2,030
Others	344	784	987	1,134	1,321
Total Liabilities	559	959	1,115	1,249	1,388
Current Liabilities	461	813	925	974	1,022
Accounts Payable	90	273	164	186	197
ST Borrowings	100	175	363	343	317
Others	271	365	398	446	507
Long-term Liabilities	99	146	190	275	366
Long-term Debts	0	125	156	229	317
Others	99	21	34	46	49
Shareholders' Equity	2,514	2,775	3,362	4,019	4,698
Common Stock	183	183	183	183	183
Capital Surplus	1,781	1,447	1,447	1,447	1,447
Retained Earnings	550	1,145	1,733	2,389	3,069
Preferred Stock	0	0	0	0	0

Source: Company data; KGI Asia Limited estimates

Key Ratios

Year to 31 Dec (Rmb mn)	2009A	2010A	2011F	2012F	2013F
Growth (% YoY)					
Sales	37.0	43.4	10.0	12.1	13.8
OP	21.0	70.2	1.0	12.7	15.0
EBITDA	23.1	74.9	6.8	14.4	14.5
NP	31.8	62.7	10.1	11.8	3.5
EPS	31.8	62.7	10.1	11.8	3.5
Profitability (%)					
Gross Margin	46.3	53.4	49.9	49.5	49.2
Operating Margin	37.4	44.3	40.7	40.9	41.3
EBITDA Margin	40.1	49.0	47.5	48.5	48.8
Net Profit Margin	30.2	34.3	34.4	34.2	31.2
ROAA	16.3	15.7	14.3	13.5	12.0
ROAE	21.5	20.2	19.1	17.8	15.6
Stability					
Gross Debt/Equity (%)	4.0	10.8	15.4	14.2	13.5
Net Debt/Equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Interest Coverage (x)	44.0	37.5	32.9	32.3	35.1
Interest & ST Debt Coverage (x)	3.7	3.5	1.9	2.2	2.8
Cash Flow Interest Coverage (x)	38.1	48.0	25.4	31.2	33.0
Cash Flow/Interest & ST Debt (x)	3.2	4.4	1.5	2.2	2.6
Current Ratio (x)	4.8	1.8	1.9	2.3	2.7
Quick Ratio (x)	4.7	1.7	1.8	2.2	2.6
Net Debt (Rmb mn)	(909)	(1,290)	(798)	(1,004)	(1,391)
Per Share Data (Rmb)					
EPS	0.16	0.26	0.28	0.32	0.33
CFPS	0.17	0.29	0.34	0.39	0.41
BVPS	1.21	1.34	1.62	1.94	2.26
SPS	0.52	0.75	0.82	0.92	1.05
EBITDA/Share	0.20	0.33	0.34	0.38	0.43
DPS	N.D.	N.D.	N.D.	N.D.	N.D.
Activity					
Asset Turnover (x)	0.5	0.5	0.4	0.4	0.4
Days Receivables	63.1	48.8	52.0	55.0	47.0
Days Inventory	23.9	16.3	17.8	18.6	18.3
Days Payable	30.4	64.2	35.1	35.4	33.0
Cash Cycle	56.6	1.0	34.7	38.3	32.4

Source: Company data; KGI Asia Limited estimates

Profit & Loss

Year to 31 Dec (Rmb mn)	2009A	2010A	2011F	2012F	2013F
Sales	1,084	1,554	1,710	1,917	2,182
Cost of Goods Sold	582	724	857	968	1,107
Gross Profit	502	830	853	949	1,074
Operating Expenses	97	141	157	164	173
Operating Profit	405	689	696	784	902
Net Interest Income	(9)	(15)	(20)	(23)	(23)
Interest Income	0	3	2	3	4
Interest Expense	9	18	23	26	27
Net Investment Income/(Loss)	0	0	0	0	0
Net other Non-op. Income/(Loss)	41	27	98	99	109
Net Extraordinaries	(39)	(51)	(55)	(58)	(61)
Pretax Income	398	651	719	803	926
Income Taxes	70	117	132	146	247
Net Profit After Extraordinaries	328	533	587	656	680
EBITDA	435	761	813	930	1,065
EPS (Rmb)	0.16	0.26	0.28	0.32	0.33

Source: Company data; KGI Asia Limited estimates

Cash Flow

Year to 31 Dec (Rmb mn)	2009A	2010A	2011F	2012F	2013F
Operating Cash Flow	352	854	571	799	895
Net Profit	328	533	587	656	680
Depreciation & Amortization	30	72	117	145	163
Change in Working Capital	(6)	249	(133)	(3)	53
Others	0	0	0	0	0
Investment Cash Flow	(325)	(1,492)	(579)	(404)	(531)
Net CAPEX	(169)	(1,052)	(377)	(257)	(344)
Change in LT Investment	0	0	0	0	0
Change in Other Assets	(156)	(440)	(203)	(147)	(187)
Free Cash Flow	28	(638)	(8)	394	364
Financing Cash Flow	1,723	(151)	232	64	66
Change in Share Capital	1,647	(273)	0	0	(0)
Net Change in Debt	100	200	219	52	63
Change in Other LT Liab.	(23)	(78)	13	12	3
Net Cash Flow	1,751	(788)	224	459	430

Source: Company data; KGI Asia Limited estimates

Rates of Return on Invested Capital

Year to 31-Dec	1- $\frac{\text{COGS}}{\text{Revenue}}$	+ $\frac{\text{Dep./Amortization}}{\text{Revenue}}$	+ $\frac{\text{SGA Exp.}}{\text{Revenue}}$	= Operating Margin		
2009A	50.9%	2.8%	8.9%	37.4%		
2010A	41.9%	4.6%	9.1%	44.3%		
2011F	43.3%	6.8%	9.2%	40.7%		
2012F	42.9%	7.6%	8.6%	40.9%		
2013F	43.3%	7.5%	7.9%	41.3%		
Year to 31-Dec	1/ $\frac{\text{Operating Working capital}}{\text{Revenue}}$	+ $\frac{\text{Net PPE}}{\text{Revenue}}$	+ $\frac{\text{Other Assets}}{\text{Revenue}}$	= Capital Turnover		
2009A	0.0	0.5	0.3	1.2		
2010A	(0.1)	0.9	0.5	0.7		
2011F	(0.0)	1.0	0.6	0.6		
2012F	(0.0)	1.0	0.6	0.6		
2013F	(0.0)	0.9	0.6	0.7		
Year to 31-Dec	Operating Margin	x	Capital Turnover	x	Cash 1 - Tax Rate	= After-tax Return on Inv. Capital
2009A	37.4%		1.2		84.0%	38.6%
2010A	44.3%		0.7		83.3%	27.6%
2011F	40.7%		0.6		83.0%	21.6%
2012F	40.9%		0.6		83.0%	22.0%
2013F	41.3%		0.7		75.0%	20.6%

Source: Company data; KGI Asia Limited estimates

KGI Locations	China	Taiwan
	<p>Shanghai Room 1907-1909, Tower A, No. 100 Zunyi Road, Shanghai, PRC 200051</p> <p>Shenzhen Room 24D1, 24/F, A Unit, Zhen Ye Building, 2014 Bao'annan Road, Shenzhen PRC 518008</p>	<p>Taipei 700 Mingshui Road, Taipei, Taiwan Telephone 886.2.2181.8888 Facsimile 886.2.8501.1691</p>
	Hong Kong	Thailand
	<p>41/F Central Plaza, 18 Harbour Road, Wanchai, Hong Kong Telephone 852.2878.6888 Facsimile 852.2878.6800</p>	<p>Bangkok 8th - 11th floors, Asia Centre Building 173 South Sathorn Road, Bangkok 10120, Thailand Telephone 66.2658.8888 Facsimile 66.2658.8014</p>

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	Underperform (U)	The stock's excess return over the next twelve months is ranked in the bottom 40% of KGI's coverage universe in the related market (e.g. Taiwan).
	Not Rated (NR)	The stock is not rated by KGI.
	Restricted (R)	KGI policy and/or applicable law regulations preclude certain types of communications, including an investment recommendation, during the course of KGI's engagement in an investment banking transaction and in certain other circumstances.
		<i>Excess return = 12M target price/current price - 1</i>
	Note	When an analyst publishes a new report on a covered stock, we rank the stock's excess return with those of other stocks in KGI's coverage universe in the related market. We will assign a rating based on its ranking. If an analyst does not publish a new report on a covered stock, its rating will not be changed automatically.

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