Report Review of Feb 2014

PhillipCapital
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Phillip Securities Research Pte Ltd

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Industry:
Local property and Others, Mainland financial, Utilities, Mainland, Mainland property, Oil and gas service, Air, Automobiles, Infrastructure, New energy & Environmental Goods

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Local retailer

We initiated coverage on Veeko International (1173.HK) and Sa Sa International (178.HK) in Feb 14.

Veeko International (1173.HK): Veeko's cosmetic business continues to expand, offsetting sluggish fashion business. For the interim results ended Sep 13, the Group's cosmetics business recorded operating profit of HKD20.9 mn, up 97.1% YoY. In the same period, operating profit for fashion business fell 81.2% YoY to HKD1.4 mn. The overall operating profit was HKD22.3 mn, up 25% YoY. The Group started cosmetics retail business since 2004, which has already accounted for 93.9% of total operating profit. We believe the Group will invest more resources in the cosmetics business in the future, to offset the downturn of fashion business. Cosmetics business has become a key growth driver for the Group. Driven by cosmetics business growth, we expect the Group's core EPS to reach HKD1.84/2.42 cents in FY14/FY15, up 32.4%/31.5% YoY, FY15 earnings will be close to FY12 level. Following the Group posted FY14 interim results, valuation discount to Sa Sa became smaller. Sa Sa is trading at FY14 P/E est. of 20.2x. Given Veeko's smaller size, weaker operational efficiency and higher operating risk, we give a target price of HKD0.33, equivalent to FY14/FY15 forecast P/E of 18x/13.6x.
Sa Sa International (178.HK): Sa Sa continued to have gross margin expansion in past few years (from 43.7% in FY09 to 46.4% in FY13). Although the gross margin may be lower than market expectation after promotion activities from mid-October of last year, management said that the fine-tune of marketing strategy would reverse the downtrend of gross margin in 4QFY14. Sa Sa recorded gross margin of 47.0% in 1HFY14 (vs. 45.7% in 1HFY13), we conservatively estimate the gross margin will expand 1.2 ppts to 46.4% in FY14. Sa Sa recorded larger operating loss in Mainland China market, the sales in 1HFY14 even dropped YoY, we expect turnaround in Mainland China market is unlikely to happen in near-term. But fortunately the operating loss was only 4-7% of operating profit in Hong Kong & Macau market. We believe the impact to overall earnings is minimal and spending power of mainland visitors will remain as Sa Sa's key growth momentum.

Sa Sa is trading at FY14 forecast P/E of 21.4x (vs. 5-year average is 20.9x), we expect Sa Sa's FY14/15 EPS to be HKD 34.6/40.6 cents, net profit's 2-year CAGR is 17.9% (vs. 29.3% CAGR for past 3-year).We give a target price of HKD8.12, based on FY15 forecast P/E of 20.0x. The major downside risks are 1.) Contraction of gross margin, 2.) Weaker spending power of mainland visitors, 3.) A significant increase in rental/staff costs.

Mainland Financial

HSI showed the upward movement in Feb 2014 after the large decrease in Jan, the index experienced the adjustment and rebounded obviously from 21,200 at the beginning of this month to 23,000 now, up over 1,000 points, and especially the market expects there are some new policies would be announced to stimulate the market development after government meetings next week. Although the PBOC tightened the market liquidity with the amount of RMB60 billion from the market recently, it stated the monetary policies would be unchanged in the short term, additionally, the market expects blue chips "T+0" in A Shares and the reform of preferred stock will be implemented this year, therefore the expectation of the market is still positive in general.

According to the sectors, the large weighted sectors such as banking, and insurance still appeared the worse performance with the iterative adjustments. Most of Chinese banks' prices increased slightly compared with the beginning of this month to varying degrees, representing the cautious view of the market for domestic banks' future performance. The main reasons are still the tightening of the liquidity in the domestic market, the slow-down of the banks' profit growth because of the decrease of NIM, and the deterioration of the banks' asset quality due to the issues of Shadow Bank, some banks' financial products appear defaults and both the amount and ratio of the NPLs continued to increase, which cause the investors to hold the cautious view of domestic banks' development. However, in Feb, only CITIC Bank recorded strong performance, the price increased from HK$3.6 at the beginning to HK$4.4 currently, up 22% approximately, this is mainly because of its better-than-expected performance, net profit increased strongly by 26% y-y approximately in 2013. We believe the banks' operating performance would maintain stable, and the valuation is quite low now. In all, we still hold a cautiously optimistic view for the banks' future performance and maintain Accumulate rating to the sector.

Mainland Telecom

The development of 4G took a further step in February. China Telecom declared that 4G was officially commercial and it would provide 4G service in nearly 100 cities in first batch. Meanwhile, China Mobile sped up building base stations and may achieve the middle-year target of providing 100 cities with base stations having commercial conditions in advance. Besides, the telecommunication tariff standard approval has been canceled, and the telephone fare is expected to fall further, and the data service will gradually replace voice business to be the main source of income of operators. Besides, the three major carriers establish independent department of mobile reselling. The development of virtual network operators may stimulate new needs for data service. Consequently, they force the basic operators to update and expand basic network.

In terms of market performance, the telecom sector keeps synchronic pace with the market, existing a trend of ascending prior to declining. Regarding specific companies, CoolPad Group, BYD Electronics, Tongda Group and other companies lead the sector, but the three carriers are still weak. Looking forwards, we think that 4G Era will lead the communications industry into a new round of prosperity. The increase of capital expenditure will support the equipment vendors and terminal manufacturers to realize considerable growth. Therefore, we still recommend the upstream to middle manufacturers like ZTE.

Mainland Property & Oil/Gas service

In February, 2014 I wrote three research reports on COSL, PKOS and BCL,which got success by unique operation model. We recommend "COSL". Benefiting from several positive factors of fundamental aspects, including definite growth of capitals of China National Offshore Oil Corporation, acceleration of the development of oil gas in South China Sea and high degree of economy among global oil gas industry, COSL Limited is equipped with solid foundation of business growth. With new platforms going into operation continuously, the business may further exceed the expectation in the future. COSL Limited is an excellent target for investors to share the rapidly growth of global and Chinese oil-gas exploration industry, as well as the best choice of the oilfield service industry among Hong Kong stocks. Above all, we give COSL Limited the rating of "buy" and the target price of 12 months reaches 27 HKD, amounting to 12.2 times of prospective P ratio in 2014.

Automobile & Air

In Feb 2014, we released one company research report (GWM 2333HK) and two sector annual reports on China automobile industry and China air industry respectively.

China's auto market moved stably in 2013, annual sales volume increased by 14% y-y with the amount of 22 million units, better than the expectation at the beginning of the year. We believe there are neutral impacts for China's passenger vehicle industry such as macro consumption environment, industrial inventory, the release of capacity, and the price level. We expect China auto market in 2014 will face a lower increase ratio, 14% for passenger vehicles and 5% for commercial vehicles, but the opportunities still exists for individual companies. We recommend BYD and Brilliance.

China air industry saw a good quantity for the relatively stale and yoy-increased growth ratio of traffic but a bad quality for the tumble ticket fare in 2013. We expected the international oil price will be changed slightly in 2014, and the growth ratio of the appreciation of RMB will slow down. Considering the slow recovery of global economy and may appear the deterioration, we believe the inflection point of the consumption upgrading cycle in domestic air industry is pending yet, but it may face the small rebound in the short run, therefore we recommend "Neutral" rating for the sector.

New energy & Environmental Goods

In this month, the stocks refer to wind power are in the fluctuation status and photovoltaic stocks price increase gradually, while environmental protection sector has a significant upward trend. There are several distributed photovoltaic projects go into operation and present some problem such as too long return term and the return uncertainty. In order to prove the attractiveness of the distributed photovoltaic projects to investors, some city and county governments introduce more subsidy policy. We believe it still needs some new policy to help to reach the 8GW goal of distributed photovoltaic projects. The 'Water pollution treatment plan' was accomplished on Feb 13th. Nation will invest 2 trillion RMB to undertake water pollution treatment and lots of new projects will start building. We recommend 'BJ ENT Water (371.HK)', the company stays in the rapid development period, the treatment capacity will have more than 50 percent increase by end of 2014. The new projects building and BOT contacts increase sharply also provide huge revenue increase to the company. More projects will be obtained under new policy in our expectation.

Fig1. Performance of Recommended stock

Time	Ticker	Company	Rating	Price on Recommendation Date	Target Price	Expected Return	Last Month Closing Price	Last Month Return	Closing Price 2M ago	1M Price Chg
2014-2-5	1173 HK Equity	Veeko	Reduce	0.35	0.33	-5.71%	0.37	5.71%	0.35	5.71%
2014-2-6	6837 HK Equity	Haitong Securities	Buy	11.04	14.42	30.62%	10.36	-6.16%	11.4	-9.12%
2014-2-7	2883 HK Equity	COSL	Buy	20.5	27	31.71%	21.05	2.68%	20.8	1.20%
2014-2-10	981 HK Equity	SMIC	Accumulate	0.8	0.9	12.50%	0.67	-16.25%	0.79	-15.19%
2014-2-12	178 HK Equity	Sa Sa	Accumulate	7.4	8.12	9.73%	7.21	-2.57%	7.43	-2.96%
2014-2-13	956 HK Equity	Suntien	Accumulate	3.22	3.56	10.56%	3.29	2.17%	3.35	-1.79%
2014-2-14	165 HK Equity	China EB	Buy	10.75	13.96	29.86%	10.24	-4.74%	10.52	-2.66%
2014-2-17	2868 HK Equity	BJ CAPITALLAND	Accumulate	3.18	3.5	10.06%	3.18	0.00%	2.65	20.00%
2014-2-18	2601 HK Equity	CPIC	Accumulate	28.4	33.65	18.49%	26.65	-6.16%	28.3	-5.83%
2014-2-21	1149 HK Equity	Anxin-China	Accumulate	1.8	2.15	19.44%	1.68	-6.67%	1.97	-14.72%
2014-2-24	2178 HK Equity	PETRO-KING	Accumulate	3.5	4	14.29%	3.52	0.57%	4.07	-13.51%
2014-2-25	2318 HK Equity	Ping An	Buy	63.05	80	26.88%	63.05	0.00%	62.9	0.24%
2014-2-26	2333 HK Equity	GWM	Accumulate	34.3	39	13.70%	35.4	3.21%	36.6	-3.28%
2014-2-27	371 HK Equity	BJ ENT Water	Accumulate	5.09	5.59	9.82%	5.56	9.23%	4.4	26.36%
2014-2-28	268 HK Equity	Kingdee	Neutral	2.93	3	2.39%	2.82	-3.75%	2.93	-3.75%

Source: PSR

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