Corporate Snippet

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Slight CSG dilution no impact on fundamentals — China Logistics

Shenzhen International (152 HK, HK$0.345) BUY (unchanged)

Target price: HK$0.45 (+30%)

Fund raising activities by CSG. Shenzhen International's (SI) 22.86%-owned associate China Southern Glass (CSG) (000012 CH) announced a series of corporate actions to raise funds for project expansion and to increase liquidity of the stock. The corporate actions include:

- Proposed A shares issuance – Issuance of 250m new A shares to approximately 10 strategic investors. The new shares will be subject to a minimum offer price of RMB7.05/share, determined based on a 10% discount of the average closing A shares price over the previous 20 trading days prior to the announcement. Foreign strategic investors will be subject to a lock up period of 36 months while other investors are subject to a 12 months lock up period. Note that the identities of the potential investors are yet to be finalised and that the Proposed Issuance is still subject to shareholders and regulatory approval.
- Bonus issue – To increase liquidity of the stock, CSG's board recommends a bonus issue of 2.5 shares for every 10 shares held by existing shareholders. Similar to the Proposed Issuance, the Bonus Issue is subject to the approval of the shareholders. Should the Bonus Issue be approved, a total of 253.9m bonus shares will be issued.

Follow through on SI. The impact of CSG's corporate actions on SI are as follows:

- Proposed Issuance will have a slight dilution effect on SI's stake in CSG. The Bonus Issue will not have any dilution effects.
- If the Bonus Issue is completed, SI's stake in CSG will decrease from 22.86% to 19.10%. If the Bonus Issue is not completed, SI's stake in CSG will decrease from 22.86% to 18.34%.
- SI will realise an accounting (non-cash) gain from the Proposed Issuance of HK$174.0m (Bonus Issue completed) and HK$208.0m (Bonus Issue not completed).
- Earnings contribution from CSG will decrease according to the extent of dilution in FY12/07F and beyond. FY12/06F impact will be minimal, depending on the timing of when the Proposed Issuance is completed.

Overall strategy in line, but dilution is a slight negative. Though the corporate actions of CSG are in line with SI's overall strategy to gradually divest from this non-core business, the dilution effects will nevertheless have a slight negative impact on SI as earnings contribution from CSG will be reduced. On the positive side, the issue price for the Proposed Issuance may provide some colour on the potential value of SI's stake in CSG. We will wait until the final details are released before making any profit adjustments, but we have conducted a scenario analysis in the meantime. Assuming the worse case scenario, where SI's stake in CSG is diluted from

Table 1: Financial summary

Year to Mar	Net profit HK$m	EPS HK$	EPS Δ %	P/E x	P/B x	EV/EBITDA x	Yield %	ROE %	ROCE %	N. Gearing %
04A	315.4	0.028	(8.2)	12.4	1.48	13.8	1.6	12.7	10.8	7.5
05A	360.3	0.032	13.8	10.9	1.26	11.1	1.6	12.5	10.6	22.2
06F	312.1	0.027	(12.9)	12.6	1.17	10.9	1.6	9.7	8.6	21.7
07F	383.1	0.034	22.7	10.2	1.07	8.9	2.0	10.9	9.5	20.3
08F	481.6	0.042	25.7	8.1	0.97	7.3	2.5	12.5	11.0	18.4

22.86% to 18.34%, our net profit forecast will be reduced by 4.7% to HK$365.9m in FY12/07F and reduced by 4.3% to HK$462.7m in FY12/08F. FY12/06F net profit will be HK$492.7m, boosted by a HK$208.0m one-off gain. The adjusted appraised NAV will be HK$0.44/share, representing a 2.2% discount on our current target price of HK$0.45/share. Note that the adjusted appraised NAV assumes an 18.34% stake in CSG and a 10% holding discount. Overall, the fundamentals of SI to become a multidisciplinary logistics conglomerate remain intact and we maintain our BUY call on the counter.