

China State Construction

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construction

Waiting for better entry point

Not Rated

Financial summary

Year to Dec	06A	07A	08A	09F	10F
Turnover (HK\$m)	10,294.810	168.311	021.413	240.815	823.4
Net Profit (HK\$m)	222.2	404.9	489.3	616.0	734.2
EPS (HK\$)	0.106	0.172	0.192	0.248	0.292
EPS Δ%	60.7	62.1	11.6	29.2	17.7
P/E (x)	10.6	6.5	6.0	5.5	4.7
P/B (x)	2.5	1.4	1.2	1.1	1.0
EV/EBITDA (x)	4.3	3.5	2.7	3.0	2.5
Yield (%)	8.4	5.8	5.5	6.6	7.8
ROE (%)	24.5	25.9	20.9	21.9	22.4
ROCE (%)	22.8	28.2	18.0	-	-
N. Gear. (%)	Cash	Cash	Cash	Cash	Cash

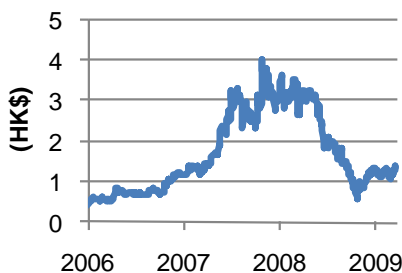
Source: Bloomberg

Price Performance

	1 mth	3 mth	12 mth
Relative to HSI (%)	-5.2	+10.1	-23.0
Actual price changes (%)	+3.0	+7.9	-49.3

	09F	10F
Consensus EPS (HK\$)	0.248	0.292
Previous forecasts (HK\$m)	-	-
Previous EPS (HK\$)	-	-

Price Chart



Kennedy Tsang / Helena Qiu

(852) 2533 3713/2533 3709

kennedytsang/ helenaqiu@sbie2capital.com

in Hong Kong should more than offset lesser contributions in UAE and India. We expect gross margins in FY12/09F to generally remain at similar levels to that in FY12/08A. The company's upside will potentially come in more infrastructure acquisitions (either from third parties or through asset injection from its parents) and tapping China's RMB4,000b fiscal stimulus package through entering into BT/BOT contracts. Management has indicated that they will target infrastructure contracts with minimum hurdle rate of IRR 12.0%.

What to do with the stock. CSCI is trading at 5.5x FY12/09F and 4.7x FY12/10F P/E on consensus prior to earnings revision. We expect the street to downgrade its estimates as well as near term concerns on it Macau market. That said, we think that the company's fundamentals remains strong, given its: 1) strong backlog; 2)

Ticker: 3311.HK	12 mth range: HK\$0.60-3.32
Price: 1.36	Market cap: US\$426.7m
Target: N/A	Daily t/o, 3 mth: US\$1.2m
	Free float %: 36.4%

Key points:

- * FY12/08A revenue up 8.4% YoY to HK\$1,021.4m while net profit up 20.9% YoY to HK\$489.3m.
- * China and HK continues to be the growth driver with a 33.0% YoY growth in sales in China and 12.5% YoY growth in HK.
- * The company's current backlog is HK\$22.8b.
- * The company's position in China and HK remains strong to offset the declining contribution from Macau, UAE and India.
- * We think that the company's fundamentals remain strong, but the catalysts will emerge from around mid-year onwards.
- * We suggest investor to wait for a better entry point to limit downside risk.

Update. FY12/08A revenue was up HK\$1,021.4m, up 8.4% YoY, net profit came in at HK\$489.3m, up 20.9% YoY. Gross margin was 8.3% up 0.8pcp YoY. Greater China continues to be the company's key driver with Hong Kong revenues up 12.5% YoY to HK\$6,191.5m and China revenues up 33.0% to HK\$882.0m. The China contribution was made up of a 19.2% YoY increase in construction related revenues and 60.3% YoY increase in infrastructure investment revenues, boosted by the two bridges in Nanchang acquired in 2008. Macau revenues grew 31.0% YoY to HK\$2,087.2m, but bookings on a HoH basis dropped 37.2% to HK\$801.9m (1H FY12/08A: HK\$1,276.3m). CSCI was awarded HK\$14.1b worth of new contracts in 2008, up 26.2% YoY and started 2009 strongly after securing HK\$4.2b contracts (Hong Kong: HK\$3.1b, China: HK\$1.0b). The company's total DPS of HK\$0.0675 represents 36.9% payout ratio. At end-FY12/08A, the group was in a net cash position of HK\$879.9m.

Our view. CSCI has entered FY12/09 in a stronger position than it did going into FY12/08 a year ago, which is good, given the uncertain climate in 2009. The company's current backlog is HK\$22.8b (beg-FY12/08: HK\$20.2b). Though the company is facing macro headwinds in Macau and non-core geographic markets such as UAE and India, it remains in a strong position in Hong Kong and China. We think that for FY12/09F, China's increased contribution (construction and infrastructure investment) should offset declining contribution from Macau while increased bookings

dominant position in Hong Kong and 3) emerging infrastructure investment segment, which has higher margin. We think that much of the company's catalysts will emerge from around mid-year onwards, where we hear news of: 1) infrastructure acquisitions; 2) BT/BOT contracts in China; 3) catalysts after Macau appoints its new Chief Executive and India has its elections and 3) progressive rollout of Hong Kong 10 major infrastructure projects. We suggest investors already with a position to a Trading HOLD, but for both short term traders yet to get into the counter and fundamental investors, we suggest to wait for a better entry point to limit downside risk.

Table 1: Revenue breakdown by region

12 months to Dec(HK\$m)	Turnover FY12/08A	Turnover FY12/07A	YoY (%)	Gross profit FY12/08A	Gross Profit FY12/07A	YoY (%)	Gross margin FY12/08A (%)	Gross margin FY12/07A (%)
Hong Kong	6,191.5	5,501.4	12.5	228.3	179.4	27.2	3.7	3.2
China (Mainland)	882.0	663.3	33.0	337.9	234.3	44.2	38.3	35.3
Macau	2,078.2	1586.8	31.0	282.3	274.1	3.0	13.6	17.2
UAE	1,797.3	2,065.4	(13.0)	56.9	52.8	7.8	3.2	2.5
India	72.4	351.4	(79.4)	4.0	25.5	(84.3)	5.5	7.3
Total	11,021.4	10,168.3	8.4	909.4	766.1	18.7	8.3	7.5

Source: Company data

Table 2: Project in Progress

12 months to Dec(HK\$b)	2007		2008		2009 Update	
	Contract value	Backlog	Contract value	Backlog	Contract value	Backlog
Hong Kong	15.48	8.27	20.48	11.94	23.62	13.68
Macau	10.86	8.78	10.42	5.06	10.42	4.26
UAE	5.88	3.05	6.08	3.22	6.08	3.07
India	0.30	0.08	-	-	-	-
China(Mainland)	0.35	0.04	1.06	0.91	2.1	1.08
Total	32.87	20.22	38.04	21.13	42.22	22.81

Source: Company data

Table 3: P & L

Year to Dec (HK\$m)	06A	07A	08A
Turnover	10,294.8	10,168.3	11,021.4
Contract cost	(9,835.8)	(9,089.6)	(9,877.8)
Other operating cost	-	(312.6)	(234.2)
Gross profit	459.0	766.1	909.4
Investment income	64.5	99.7	33.5
Other income	13.3	30.2	44.5
Selling and distribution costs	(4.8)	(10.7)	(17.8)
Administrative expenses	(249.7)	(332.0)	(394.0)
Other expenses	(16.5)	(29.9)	(2.8)
Reversal of impairment loss of properties held for sales			18.3
Impairment loss of investment properties			(3.0)
Impairment loss of available for sale investment			(6.7)
Operating profit	265.8	523.4	581.4
Financial costs	(1.6)	(1.8)	(20.1)
Share of loss of an associate	6.9	8.8	9.4
Pre-tax profit	271.0	530.3	570.7
Tax	(49.2)	(82.4)	(66.3)
Minority interests	0.3	(43.1)	(15.1)
Net profit	222.2	404.9	489.3

Source: Company data

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