

Sino Union Energy Investment

Building a vertical oil and gas platform

to summarize...

- Adjusted net profit of 9-months ended Dec 2011 was HK\$1.9m
- Sole listed platform of SOE Yanchang Petroleum Group; listco name changed
- Developing into vertical integrated oil and gas investment platform
- Expecting to raise refined oil products sales to 0.6m in 2012
- SUEI in the progress of exploration in Madagascar
- Current valuation at 0.40x P/B by the end of 2011

2011A results summary. Sino Union Energy Investment (SUEI) announced results ended Dec 2011. While year end change to Dec, the company announced 9-months results ended Dec 2011 and 12-months results ended Mar 2011. Revenue for the latest 9-months was HK\$512.2m with gross margin at 6.5%. With non-cash equity-settled share option expenses of HK\$145.6m and impairment loss of intangible assets at HK\$5.6m, net loss was HK\$149.3m for the 9-month period. Adjusted net profit was HK\$1.9m. At the same time, SUEI announced to change its name to "Yanchang Petroleum International Limited".

Table 1. Annual results overview

HK\$m	FY03/11A	9-months Dec 2011A
Revenue	1,020.8	512.2
Gross profit	35.1	33.4
EBIT	25.3	(137.2)
EBT	25.3	(138.8)
Net profit	23.0	(149.3)

Source: SBI E2-Capital

Extending from downstream business to upstream oilfield operation. In Nov 2011, SUEI completed acquisition of 70% of Henan Yanchang Petroleum Sales which engages in distribution of refined oil products in China. It has 120,000 m³ storage tank, a private railway line of 2,500 meters and a retail network of 10 gas stations. With supply support of refined oil products and strategic cooperation in the upper-stream oil and gas exploration in Madagascar by Yanchang Petroleum, SUEI is expected to become a strong investment platform from upstream to midstream and downstream on oil and gas operation in China and overseas.

Sole listed platform of State-owned Enterprise, Yanchang Petroleum. Shaanxi Yanchang Petroleum Group is a state-owned enterprise directly attached to Shaanxi People's Provincial Government. The group was founded in 1905 and it is one of the four qualified enterprises for oil and gas exploration in China together with PetroChina (0857 HK), Sinopec (0386 HK) and CNOOC (0883 HK). On 1 Apr 2012, 3 deputy general managers of Yanchang Petroleum Group became ED of the listco.

Table 2. Shareholding structure of BHI

Shareholder	Prior to derivatives conversion	Upon full conversion
Shaanxi Yanchang Petroleum	13.4%	23.8%
Chairman Zhuo Ze Fan	23.9%	20.3%
ED Liu Xingyuan	5.2%	4.4%
Goldern Soar	0%	2.6%
Public	57.5%	48.9%
Total	100%	100%

Source: HKEx

Ticker	0346 HK
Rating	Not Rated
Price (HK\$)	0.52
Target Price (HK\$)	n.a.
12m Price Range (HK\$)	0.44 - 0.81
Market cap. (US\$m)	456.3
Daily t/o (US\$m)	0.3
Free float (%)	53.0

Financial summary

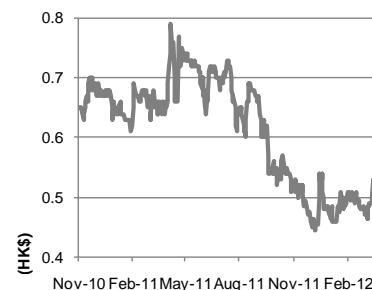
Year to Dec	12-month ended Mar 2011A	9-month ended Dec 2011A
Turnover (HK\$m)	1,020.7	512.2
Net Profit (HK\$m)	23.0	(149.3)
EPS (HK\$)	0.0037	(0.0234)
P/E (x)	140.5	n.a.
P/B (x)	0.41	0.4
EV/EBITDA (x)	132.4	n.a.
Yield (%)	n.a.	n.a.
ROE (%)	0.3	n.a.
ROCE (%)	0.3	n.a.
N. Gear. (%)	Cash	1.5

Source: SBI E2-Capital

	11F	12F	13F
Consensus EPS (HK\$)	-	-	-
Previous earnings (HK\$m)	-	-	-
Previous EPS (HK\$)	-	-	-

Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	10.3	(13.4)	(9.7)
Actual price changes (%)	4.5	(2.1)	(23.6)



Source: Bloomberg

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Current sales breakdown and expansion prospects. By the end of 2011, sales income of SUEI was solely by contributed of trading of oil related products. With approval of PetroChina (0857 HK), SUEI is to construct a sub-pipeline connecting Zhengzhou distribution station of Lanzhou-Zhengzhou-Changsha refined oil major pipeline. Upon completion of this 23km long pipeline, transportation and sales of refined oil products in Henan Province will be improved. While current demand of refined oil products in Henan Province is around 10m tonnes a year, the management expects to raise refined oil sales to 0.6m tonnes in 2012 and up to 1.5m in 2013 with the supply from Yanchang Petroleum. On the other hand, while the major asset of the SUEI was in Madagascar, this upper stream segment is yet to contribute sales in the future after exploration and construction work. Table 3 shows current sales mix as well as asset geographical location by the end of Dec 2011.

Table 3. Current sales and asset

HK\$m	12 months ended Mar 2011	9 months ended Dec 2011
Sales breakdown		
Trading of oil related products	1,020.8	512.2
Oil and gas exploration and operation	0	0
	Mar 2011	Dec 2011
Asset geographical location		
China	0.02	475.2
Hong Kong	2.2	53.5
Madagascar	8,531.9	8,664.8

Source: SBI E2-Capital

Upstream business in Madagascar. In Madagascar, there are already 225 offshore oil and gas exploration blocks in addition to onshore blocks which has attracted foreign oil companies including Exxon Mobil, Sterling Energy, Total, Essar Varun and PetroChina. SUEI has two oil and gas blocks in the southwestern part of Madagascar. For both of the blocks SUEI have exploitation and operation rights of 25 years+. According to Netherland, Sewell & Associates technical assessment reports in 2007 and 2008, SUEI oilfield block 3113 and 2104 together showed 5.68b barrels to 10.54b barrels unrisksed gross original oil-in-place. By end of 2011, SUEI proceeded to evaluation stage of its drilling program for block 3113. In fact, at west of block 3113, block 3112 was confirmed by Madagascar Southern Petroleum to contain high pressure natural gas at a depth of 2,755 meters. SUEI completed second batch of 3 wells by the end of last year. There is good chance of positive results this year, according to the management. On the other hand, the management indicated that they obtained satisfactory results in the drilling works of 5 wells with depth between 450 and 2,153 meters for block 2104. With airport and seaport access within 100km, oil and gas production is of high economic value upon completion of drilling and construction in the future.

Table 4. Madagascar oilfield blocks statistics

<u>Oilfield block 3113</u>		
Total area		8,320km ²
Unrisksed gross original oil-in-lace		2.03b to 6.89b barrels
Royalty – oil		8% to 20%
Oil profit share after royalty and expenses	SUEI (43.4%), Yanchang Petroleum (32.8%) and ECO Energy (23.8%)	
Status		Single-well evaluation studies
<u>Oilfield block 2104</u>		
Total area		20,100km ²
Unrisksed gross original oil-in-lace		3.65b barrels
Royalty – oil		8% to 20%
Oil profit share after royalty and expenses		SUEI (100%)
Status		Analyzing results in drilling works of five wells

Source: SBI E2-Capital

Valuation. The counter is currently trading at 0.40x P/B based on HK\$8,966m net equity (including HK\$8,546.7m exploration and evaluation assets) by the end of 2011, subject to re-rating on its eventual emergence of upstream oil and gas operation.

Table 5. Balance sheet summary

HK\$m	Mar 2011	Dec 2011
<u>Non-current assets</u>		
Property, plant and equipment	3.6	143.9
Intangible asset	40.0	316.7
Exploration and evaluation assets	8,481.8	8,546.7
Other non-current assets	8.7	186.3
<u>Current assets</u>		
Trade and other receivables	277.4	31.7
Inventories	0	106.1
Pledged deposits and cash	103.0	78.8
Other current assets	1.4	0
<u>Non-current liabilities</u>		
Deferred taxation	1.3	85.4
<u>Current liabilities</u>		
Trade and bills payables	89.7	120.3
Borrowings	0	130.0
Promissory note	0	84.7
Other current liabilities	14.8	23.3
<u>Equity</u>	<u>8,760.0</u>	<u>8,966.4</u>

Source: SBI E2-Capital

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