



Wanhua Chemical Group (600309.SS)

Earnings review: In line FY19 results, seeking new growth drivers, Neutral

Neutral

600309.SS 12m Price Target: **Rmb48.00** Price: **Rmb40.00** Upside: **20.0%**

Wanhua Chemical just reported FY19 results with net income of Rmb10bn, reaching the company's target made in early 2019. Both EBIT and EPS are in line with our GS estimates. The company is only committed to 40% dividend payout and cut the dividend by 35% to Rmb1.3/sh (vs. GSe of 1.68). Wanhua has reiterated the company's commitment in seeking new growth drivers (outside of the traditional polyurethane business) and developing the petrochemical business (access high end olefin market). We expect the key investor debate to be around growth sustainability (both MDI and petrochemical), the pace of product prices recovery and the appropriate worst-case scenario (1Q2020 being the near term catalyst). We revised up our 12-m EV/EBITDA based target price by 1% to Rmb48.00/sh.

FY19 results in line; strong petrochemical offset weak specialty chem; disappointed dividend

Wanhua Chemical reported in line FY19 results. The polyurethane segment disclosure is broadly in line with our expectation, achieving average MDI utilization of 85% and TDI of 76%. The main surprise is the petrochemical business, achieving higher-than-expected utilization (FY19 utilization of 106%, vs. 94% in FY18). This offset the weaker-than-expected specialty chemical business (lower margin as revenue/volume grew further). Despite an improved operating cash flow, Wanhua decided to cut the payout ratio from 52% in 2018 to 40% in 2019 and cut the dividend per share by 35% to Rmb1.3/sh. We believe this leaves room for heavier capex spending for new projects in 2020 and 2021E.

New project pipelines under construction

Wanhua revised the list of projects under construction and the plants commissioning timeline. They are aiming to commission PC

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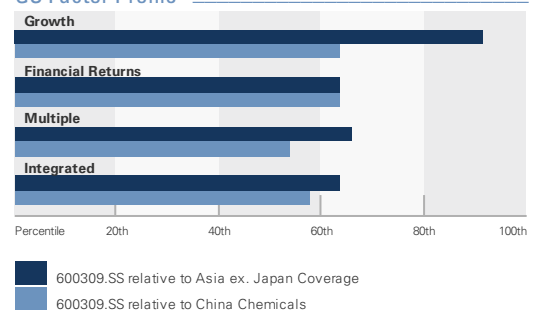
Key Data

Market cap: Rmb125.6bn / \$17.7bn
Enterprise value: Rmb160.9bn / \$22.7bn
3m ADTV: Rmb1.1bn / \$154.9mn
China
China Chemicals
M&A Rank: 3
Leases incl. in net debt & EV?: No

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue (Rmb mn) New	68,050.7	64,235.4	86,531.8	96,003.2
Revenue (Rmb mn) Old	65,086.7	58,391.1	84,568.8	95,171.2
EBITDA (Rmb mn)	17,156.3	15,929.6	26,528.2	28,945.1
EPS (Rmb) New	3.23	2.46	4.70	4.92
EPS (Rmb) Old	3.27	2.48	4.49	4.85
P/E (X)	13.3	16.3	8.5	8.1
P/B (X)	3.2	2.7	2.3	1.9
Dividend yield (%)	3.0	2.5	4.7	5.0
CROCI (%)	20.2	13.7	18.6	17.7
	12/19	3/20E	6/20E	9/20E
EPS (Rmb)	0.71	0.37	0.66	0.92

GS Factor Profile



Source: Company data, Goldman Sachs Research estimates.
See disclosures for details.

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Neutral

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Rating since Aug 5, 2019

Ratios & Valuation

	12/19	12/20E	12/21E	12/22E
P/E (X)	13.3	16.3	8.5	8.1
P/B (X)	3.2	2.7	2.3	1.9
FCF yield (%)	6.0	(4.3)	4.2	5.9
EV/EBITDAR (X)	9.4	10.1	6.1	5.6
EV/EBITDA (excl. leases) (X)	9.4	10.1	6.1	5.6
CROCI (%)	20.2	13.7	18.6	17.7
ROE (%)	25.2	17.3	28.7	25.6
Net debt/equity (%)	56.3	68.2	58.1	47.5
Net debt/equity (excl. leases) (%)	56.3	68.2	58.1	47.5
Interest cover (X)	9.7	7.1	11.7	12.4
Days inventory outst, sales	47.0	50.3	43.5	45.9
Receivable days	58.4	46.3	39.2	42.8
Days payable outstanding	103.7	142.1	125.3	133.9
DuPont ROE (%)	23.1	15.8	25.3	22.6
Turnover (X)	0.7	0.6	0.7	0.7
Leverage (X)	2.2	2.3	2.2	2.0
Gross cash invested (ex cash) (Rmb)	94,464.8	113,106.8	129,146.7	144,598.5
Average capital employed (Rmb)	65,447.6	75,464.8	87,289.5	96,596.5
BVPS (Rmb)	13.49	14.96	17.77	20.71

Growth & Margins (%)

	12/19	12/20E	12/21E	12/22E
Total revenue growth	(6.6)	(5.6)	34.7	10.9
EBITDA growth	(27.2)	(7.2)	66.5	9.1
EPS growth	(43.3)	(23.8)	91.1	4.8
DPS growth	(35.0)	(23.8)	91.1	4.8
EBIT margin	18.5	16.5	23.6	22.7
EBITDA margin	25.2	24.8	30.7	30.2
Net income margin	14.9	12.0	17.0	16.1

Price Performance



Income Statement (Rmb mn)

	12/19	12/20E	12/21E	12/22E
Total revenue	68,050.7	64,235.4	86,531.8	96,003.2
Cost of goods sold	(44,396.8)	(41,544.4)	(52,595.2)	(57,605.2)
SG&A	(5,921.5)	(6,217.6)	(6,675.9)	(8,640.3)
R&D	-	-	-	-
Other operating inc./(exp.)	(576.0)	(543.7)	(732.4)	(812.6)
EBITDA	17,156.3	15,929.6	26,528.2	28,945.1
Depreciation & amortization	(4,600.8)	(5,300.9)	(6,144.3)	(7,104.8)
EBIT	12,555.5	10,628.7	20,384.0	21,840.3
Net interest inc./(exp.)	(1,130.6)	(1,399.0)	(1,607.5)	(1,619.9)
Income/(loss) from associates	88.0	107.6	107.6	107.6
Pre-tax profit	12,260.4	9,837.3	19,284.1	20,728.0
Provision for taxes	(1,667.0)	(1,751.3)	(3,835.3)	(4,536.5)
Minority interest	(463.3)	(363.9)	(695.2)	(728.6)
Preferred dividends	-	-	-	-
Net inc. (pre-exceptionals)	10,130.0	7,722.1	14,753.6	15,462.9
Post-tax exceptionals	-	-	-	-
Net inc. (post-exceptionals)	10,130.0	7,722.1	14,753.6	15,462.9
EPS (basic, pre-exception) (Rmb)	3.23	2.46	4.70	4.92
EPS (diluted, pre-exception) (Rmb)	3.23	2.46	4.70	4.92
EPS (basic, post-exception) (Rmb)	3.23	2.46	4.70	4.92
EPS (diluted, post-exception) (Rmb)	3.23	2.46	4.70	4.92
DPS (Rmb)	1.30	0.99	1.89	1.98
Div. payout ratio (%)	40.3	40.3	40.3	40.3

Balance Sheet (Rmb mn)

	12/19	12/20E	12/21E	12/22E
Cash & cash equivalents	4,566.3	5,982.6	6,395.6	7,833.8
Accounts receivable	8,379.8	7,919.4	10,668.3	11,836.0
Inventory	8,586.9	9,105.6	11,527.7	12,625.8
Other current assets	1,950.6	1,950.6	1,950.6	1,950.6
Total current assets	23,483.6	24,958.2	30,542.2	34,246.1
Net PP&E	61,544.6	74,646.7	83,905.4	92,203.6
Net intangibles	6,694.4	6,291.4	5,888.4	5,485.3
Total investments	892.3	999.9	1,107.5	1,215.2
Other long-term assets	4,250.5	4,250.5	4,250.5	4,250.5
Total assets	96,865.3	111,146.7	125,694.0	137,400.8
Accounts payable	16,410.8	15,934.9	20,173.5	22,095.1
Short-term debt	23,358.2	33,358.2	34,358.2	34,358.2
Short-term lease liabilities	-	-	-	-
Other current liabilities	5,030.6	5,030.6	5,030.6	5,030.6
Total current liabilities	44,799.6	54,323.6	59,562.3	61,483.9
Long-term debt	5,962.6	5,962.6	5,962.6	5,962.6
Long-term lease liabilities	-	-	-	-
Other long-term liabilities	2,171.9	1,954.7	1,759.2	1,583.3
Total long-term liabilities	8,134.5	7,917.3	7,721.8	7,545.9
Total liabilities	52,934.1	62,240.9	67,284.1	69,029.8
Preferred shares	-	-	-	-
Total common equity	42,364.1	46,974.7	55,783.7	65,016.1
Minority interest	1,567.2	1,931.0	2,626.2	3,354.8
Total liabilities & equity	96,865.3	111,146.7	125,694.0	137,400.8
Net debt, adjusted	24,754.4	33,338.2	33,925.2	32,487.0

Cash Flow (Rmb mn)

	12/19	12/20E	12/21E	12/22E
Net income	10,130.0	7,722.1	14,753.6	15,462.9
D&A add-back	4,600.8	5,300.9	6,144.3	7,104.8
Minority interest add-back	463.3	363.9	695.2	728.6
Net (inc)/dec working capital	8,950.6	(534.3)	(932.3)	(344.2)
Other operating cash flow	1,788.3	(324.8)	(303.1)	(283.6)
Cash flow from operations	25,932.9	12,527.7	20,357.6	22,668.6
Capital expenditures	(17,814.8)	(18,000.0)	(15,000.0)	(15,000.0)
Acquisitions	(6,615.0)	-	-	-
Divestitures	6,063.0	-	-	-
Others	0.0	-	-	-
Cash flow from investing	(18,366.9)	(18,000.0)	(15,000.0)	(15,000.0)
Repayment of lease liabilities	-	-	-	-
Dividends paid (common & pref)	(8,249.2)	(3,111.5)	(5,944.7)	(6,230.5)
Inc/(dec) in debt	(909.2)	10,000.0	1,000.0	0.0
Other financing cash flows	(81.5)	0.0	0.0	0.0
Cash flow from financing	(9,240.0)	6,888.5	(4,944.7)	(6,230.5)
Total cash flow	(1,673.9)	1,416.3	413.0	1,438.2
Free cash flow	8,118.1	(5,472.3)	5,357.6	7,668.6

Source: Company data, Goldman Sachs Research estimates.

phase 2 130kt and ethylene plant in 2020. Other pending projects include their newly set up Fujian MDI project, Guangdong TPU project, BC optimization plan; Ningbo upgrade plans, etc. In light of the limited progress in the US new plant investment, Wanhua booked an impairment loss to the initial investment amount of Rmb310mn.

Commitment in seeking new growth drivers

Wanhua Chemical reiterate the company's commitment in seeking new growth drivers. A majority of the discussion/emphasis is on their petrochemical and specialty chemical businesses (instead of the traditional polyurethane business). In petrochemical, Wanhua said that it would like to increase the product catalog and leverage the soon to be commissioned ethylene plant to grow and expand their high-end olefin products. In specialty chemical, Wanhua mentioned their progress in developing PC, PMMA, Nylon-12 and Citral production. The company is also actively researching the production and application of bio-polymer, degradable plastic, etc.

Earnings and valuation

We revised our Wanhua's 2020-2022 EPS estimates by -1%/5%/1% to incorporate the FY19 results and the latest project pipelines. We apply 8.0X target multiple of 2H20E-1H21E total EBITDA (unchanged methodology) to derive our 12-month target price of Rmb48.00/sh (+1%).

Key risks

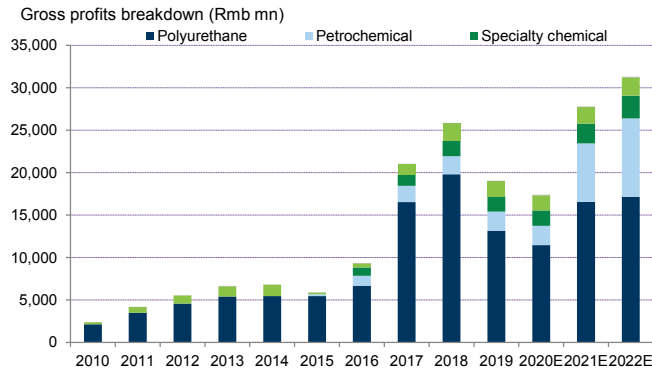
(+/-) Product margin; supply disruption; project delays; feedstock cost volatility; operational risks; R&D success.

Exhibit 1: Wanhua Chemical's summary financial

Summary Financials		vs. GSe					vs. pcp									
		CY17	CY18	CY19	FY19	Var	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19	4Q18	4Q19
		Act.	Act.	Act.	Est.	%	Act.	Act.	Act.	Act.	Act.	Act.	Act.	Act.	Act.	
Revenue	Rmb mn	53,123	72,837	68,051	65,087	5%	13,602	16,452	15,869	14,698	15,952	15,587	17,000	19,511	33%	15%
COGS (DD&A excluded)	Rmb mn	-28,848	-42,511	-44,397	-41,607	7%	-7,749	-10,246	-11,018	-11,100	-11,084	-10,545	-12,434	-14,935	35%	20%
Gross profits	Rmb mn	24,276	30,326	23,654	23,480	1%										
DD&A	Rmb mn	-3,186	-3,982	-4,601	-4,360	6%										
Segment profit	Rmb mn	21,090	26,344	19,053	19,120	0%	5,853	6,206	4,851	3,598	4,868	5,042	4,566	4,577	27%	0%
Polyurethane	Rmb mn	16,530	19,805	13,170	13,280	-1%										
Petrochemical	Rmb mn	1,910	2,133	2,242	1,785	26%										
Specialty chemical	Rmb mn	1,322	1,797	1,817	1,996	-9%										
Others	Rmb mn	1,294	2,092	1,776	1,960	-9%										
SG&A	Rmb mn	-3,452	-5,936	-5,922	-5,532	7%	-799	-1,060	-1,311	-1,163	-1,371	-1,505	-1,403	-1,643	41%	17%
Other operating expenses	Rmb mn	-475	-822	-576	-521	11%	-150	-164	-130	-102	-154	-120	-108	-194	89%	79%
EBITDA	Rmb mn	20,349	23,568	17,156	17,427	-2%									n.m.	n.m.
EBIT	Rmb mn	17,163	19,585	12,556	13,067	-4%	4,904	4,981	3,410	2,332	3,343	3,418	3,055	2,740	17%	-10%
Shares of profit of associates & JVs	Rmb mn	105	120	88	116	-24%	30	24	24	15	20	35	32	1		
Interest income/(expenses)	Rmb mn	-929	-1,048	-1,080	-1,040	4%	-248	-173	-232	-143	-271	-308	-192	-308	116%	61%
Non-operating income/(expenses)	Rmb mn	412	839	697	1,000	-30%	498	288	178	87	498	282	117	-200	-330%	-271%
Pre-Tax Profit	Rmb mn	16,750	19,495	12,260	13,143	-7%	5,184	5,121	3,381	2,292	3,589	3,426	3,012	2,233	-3%	-26%
Tax	Rmb mn	-3,440	-3,423	-1,667	-2,345	-29%	-1,051	-1,025	-753	-320	-655	-484	-607	79	-125%	-113%
Non-controlling interest	Rmb mn	-2,175	-506	-463	-540	-14%	-588	-692	-557	-382	-138	-117	-127	-81	-79%	-36%
NPAT (reported)	Rmb mn	11,135	15,566	10,130	10,259	-1%	3,546	3,404	2,071	1,589	2,796	2,825	2,278	2,231	40%	-2%
Underlying EPS	Rmb/sh	4.09	3.88	3.23	3.27	-1%	1.30	1.25	0.76	0.58	0.89	0.90	0.73	0.71	22%	-2%
Dividend (tax inclusive)	Rmb/sh	1.50	2.00	1.30	1.68	-23%				2.00				1.30	n.m.	n.m.
Payout ratio	%	37%	52%	40%	52%											

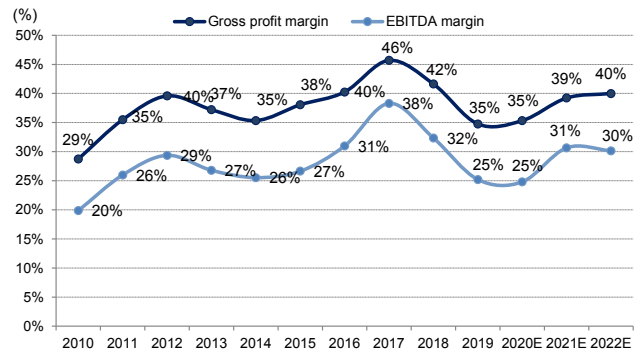
Source: Company data, Gao Hua Securities Research

Exhibit 2: We expect a higher contribution from petrochemical business starting 2021E



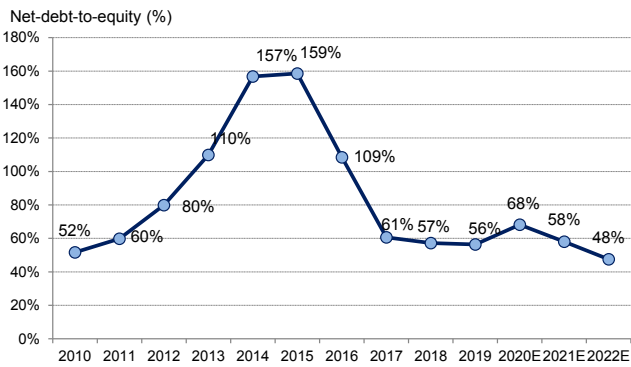
Source: Company data, Gao Hua Securities Research

Exhibit 3: We believe margin to reach bottom in 2019/2020



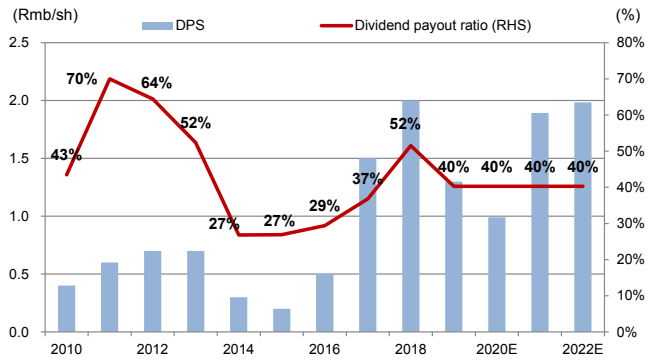
Source: Company data, Gao Hua Securities Research

Exhibit 4: We believe the new ethylene plant will lift the gearing temporarily



Source: Company data, Gao Hua Securities Research

Exhibit 5: We now forecast 40% dividend payout during 2020-2022E



Source: Company data, Gao Hua Securities Research

Disclosure Appendix

Reg AC

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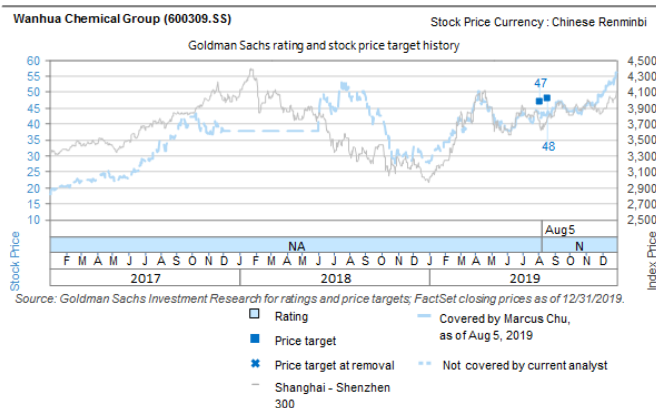
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