

Neutral

China Molybdenum Co. (603993.SS)

Earnings Review: 1H above expectations on lower tax and minorities; incorporating possibility of super tax impact into valuation; upgrade

603993.SS	12m Price Target: Rmb5.60	Price: Rmb4.98	Upside: 12.4%
3993.HK	12m Price Target: HK\$3.70	Price: HK\$3.34	Upside: 10.8%

China Moly 1H18 NP came in at Rmb3.123bn, with EPS at Rmb0.145, up 192% yoy. Excluding one-offs, recurring NP was Rmb3.16bn, up 199% yoy, higher than our estimates mainly due to lower tax from deferred income tax benefit and lower minorities.

Tenke delivered 84kt of copper in 1H18A, 15% lower than expected, but cobalt output reached 9kt, 8% higher than expected. Total gross profit from Tenke was mostly in line, as higher revenue was offset by higher cost. NPM delivered 17kt of copper output, mostly in line. Unit COGS per copper volume (excluding credit) from Tenke was Rmb53,489/t for 1H18, on our estimates, much higher than expectations due to lower copper volumes in the period, while reported C1 cost was -US\$1.04/lb, lower than full year guidance of -US\$0.42/lb due to higher cobalt prices and volume in 1H18. Unit COGS per copper volume (excluding credit) from NPM was Rmb30,503/t, flat yoy, lower than our expectation. Operating cash flow was strong at Rmb5.4bn, up 55% yoy, but was partly offset by Rmb3.9bn in investment cash flow. Net gearing reached 10%, flat versus 6 months ago.

The DRC President signed a new mining code (which includes potential super tax charges) into law in June 2018, and the royalty tax on copper and cobalt has increased from 2% to 3.5% since mid 2018. The specifics of how a super tax would be implemented are still under negotiation, as it would vary from mine to mine due to different metal price assumptions in feasibility studies and it would take time (potentially one year) to finalise. We estimate full execution of the tax as currently proposed could lead to a 34-37% negative impact on 2019E-2020E profit. According to the company, it is still negotiating with the DRC government to partially ease the

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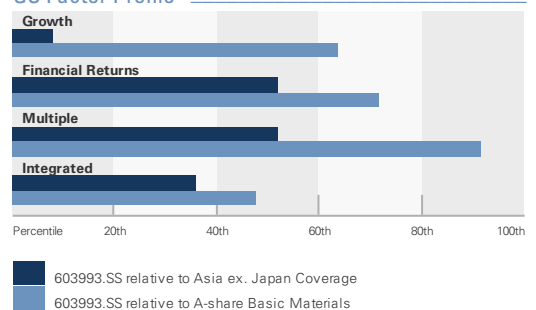
Key Data

Market cap: Rmb107.6bn / \$15.8bn
Enterprise value: Rmb113.3bn / \$16.6bn
3m ADTV: Rmb671.9mn / \$100.5mn
China
A-share Basic Materials
M&A Rank: 3

GS Forecast

	12/17	12/18E	12/19E	12/20E
Revenue (Rmb mn) New	24,147.6	28,316.2	28,171.0	28,003.3
Revenue (Rmb mn) Old	24,147.6	25,966.6	26,069.6	25,358.6
EBITDA (Rmb mn)	11,394.5	13,974.3	13,743.2	13,370.7
EPS (Rmb) New	0.14	0.25	0.22	0.23
EPS (Rmb) Old	0.14	0.21	0.22	0.22
P/E (X)	40.0	19.6	22.6	22.1
P/B (X)	3.2	2.6	2.5	2.4
Dividend yield (%)	1.3	3.1	2.7	2.7
CROCI (%)	19.9	20.3	20.1	20.7
	12/17	6/18	12/18E	--
EPS (Rmb)	0.10	0.14	0.11	--

GS Factor Profile



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

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Rating since Aug 29, 2018

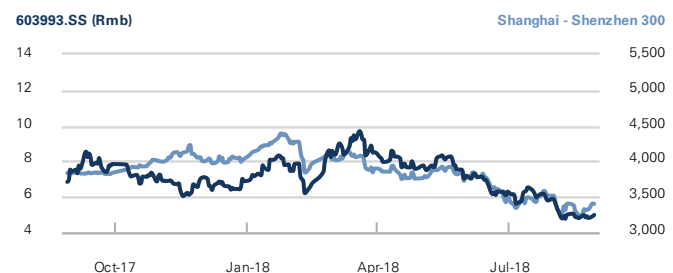
Ratios & Valuation

	12/17	12/18E	12/19E	12/20E
P/E (X)	40.0	19.6	22.6	22.1
P/B (X)	3.2	2.6	2.5	2.4
FCF yield (%)	2.2	7.1	7.8	7.6
EV/EBITDA (X)	10.5	8.1	7.9	7.8
CROCI (%)	19.9	20.3	20.1	20.7
ROE (%)	9.6	13.7	11.1	11.0
Net debt/equity (%)	8.2	(5.6)	(16.4)	(26.4)
Interest cover (X)	3.1	4.4	4.8	5.6
Days inventory outst, sales	81.5	73.4	73.5	73.6
Receivable days	47.7	48.9	47.8	47.8
Days payable outstanding	28.8	27.4	32.1	32.1
DuPont ROE (%)	5.9	10.8	8.9	8.6
Turnover (X)	0.2	0.3	0.3	0.3
Leverage (X)	2.1	2.0	1.8	1.7

Growth & Margins (%)

	12/17	12/18E	12/19E	12/20E
Total revenue growth	247.5	17.3	(0.5)	(0.6)
EBITDA growth	392.9	22.6	(1.7)	(2.7)
EPS growth	142.3	77.0	(13.2)	2.5
DPS growth	117.1	100.7	(13.2)	2.5
EBIT margin	28.0	34.1	33.8	33.7
EBITDA margin	47.2	49.4	48.8	47.7
Net income margin	11.3	19.3	16.9	17.4

Price Performance



	3m	6m	12m
Absolute	(33.9)%	(42.0)%	(25.2)%
Rel. to the Shanghai - Shenzhen 300	(25.4)%	(31.3)%	(15.5)%

Source: FactSet. Price as of 28 Aug 2018 close.

Income Statement (Rmb mn)

	12/17	12/18E	12/19E	12/20E
Total revenue	24,147.6	28,316.2	28,171.0	28,003.3
Cost of goods sold	(15,211.9)	(16,024.6)	(15,965.2)	(15,886.1)
SG&A	(1,373.9)	(1,611.1)	(1,602.9)	(1,593.3)
R&D	-	-	-	-
Other operating inc./exp.)	92.4	92.4	92.4	92.4
EBITDA	11,394.5	13,974.3	13,743.2	13,370.7
Depreciation & amortization	(4,630.6)	(4,309.4)	(4,224.1)	(3,925.0)
EBIT	6,763.9	9,664.9	9,519.1	9,445.7
Net interest inc./exp.)	(1,417.0)	(975.9)	(684.6)	(386.6)
Income/(loss) from associates	30.2	30.2	30.2	30.2
Pre-tax profit	5,381.8	8,672.8	8,864.6	9,089.3
Provision for taxes	(1,786.2)	(2,359.5)	(2,925.3)	(2,999.5)
Minority interest	(867.8)	(838.8)	(1,187.9)	(1,218.0)
Preferred dividends	-	-	-	-
Net inc. (pre-exceptionals)	2,727.8	5,474.5	4,751.5	4,871.9
Post-tax exceptionals	-	-	-	-
Net inc. (post-exceptionals)	2,727.8	5,474.5	4,751.5	4,871.9
EPS (basic, pre-exception) (Rmb)	0.14	0.25	0.22	0.23
EPS (diluted, pre-exception) (Rmb)	0.14	0.25	0.22	0.23
EPS (basic, post-exception) (Rmb)	0.14	0.25	0.22	0.23
EPS (diluted, post-exception) (Rmb)	0.14	0.25	0.22	0.23
DPS (Rmb)	0.08	0.15	0.13	0.14
Div. payout ratio (%)	53.1	60.2	60.2	60.2

Balance Sheet (Rmb mn)

	12/17	12/18E	12/19E	12/20E
Cash & cash equivalents	26,508.8	31,085.0	30,925.6	30,741.5
Accounts receivable	3,895.3	3,698.5	3,679.6	3,657.7
Inventory	5,705.5	5,682.3	5,661.2	5,633.2
Other current assets	2,939.2	2,939.2	2,939.2	2,939.2
Total current assets	39,048.8	43,405.0	43,205.6	42,971.6
Net PP&E	24,234.9	24,478.1	22,694.6	21,106.3
Net intangibles	21,536.2	19,983.7	18,543.1	17,206.3
Total investments	1,136.4	1,136.4	1,136.4	1,136.4
Other long-term assets	11,881.0	11,881.0	11,881.0	11,881.0
Total assets	97,837.2	100,884.1	97,460.6	94,301.6
Accounts payable	1,000.4	1,408.3	1,401.1	1,392.7
Short-term debt	6,258.5	5,838.6	4,586.3	3,267.9
Other current liabilities	6,244.1	6,244.1	6,244.1	6,244.1
Total current liabilities	13,503.1	13,491.0	12,231.5	10,904.8
Long-term debt	24,033.9	22,421.1	17,612.2	12,549.4
Other long-term liabilities	14,391.1	14,391.1	14,391.1	14,391.1
Total long-term liabilities	38,425.0	36,812.3	32,003.3	26,940.5
Total liabilities	51,928.1	50,303.3	44,234.9	37,845.3
Preferred shares	-	-	-	-
Total common equity	38,157.2	41,990.1	43,447.1	45,459.7
Minority interest	7,752.0	8,590.7	9,778.6	10,996.6
Total liabilities & equity	97,837.2	100,884.1	97,460.6	94,301.6
Gross cash invested (ex cash)	56,833.6	54,575.1	51,232.9	47,967.2
Net debt, adjusted	3,783.7	(2,825.3)	(8,727.0)	(14,924.2)
Average capital employed	54,437.9	48,724.2	46,127.1	43,015.4
BVPS (Rmb)	1.77	1.94	2.01	2.10

Cash Flow (Rmb mn)

	12/17	12/18E	12/19E	12/20E
Net income	2,727.8	5,474.5	4,751.5	4,871.9
D&A add-back	4,630.6	4,309.4	4,224.1	3,925.0
Minority interest add-back	867.8	838.8	1,187.9	1,218.0
Net (inc)/dec working capital	(2,004.9)	627.9	32.8	41.6
Other operating cash flow	4,935.2	5,474.5	4,751.5	4,871.9
Cash flow from operations	8,428.8	11,250.5	10,196.2	10,056.5
Capital expenditures	(5,900.8)	(3,000.0)	(1,000.0)	(1,000.0)
Acquisitions	(5,900.8)	(3,000.0)	(1,000.0)	(1,000.0)
Divestitures	-	-	-	-
Others	1,791.5	-	-	-
Cash flow from investing	(4,109.2)	(3,000.0)	(1,000.0)	(1,000.0)
Dividends paid (common & pref)	(591.1)	(1,641.5)	(3,294.5)	(2,859.3)
Inc/(dec) in debt	(4,524.0)	(2,032.7)	(6,061.2)	(6,381.2)
Other financing cash flows	12,487.1	0.0	0.0	0.0
Cash flow from financing	7,372.0	(3,674.3)	(9,355.6)	(9,240.5)
Total cash flow	16,538.5	4,576.2	(159.4)	(184.1)
Free cash flow	2,528.0	8,250.5	9,196.2	9,056.5

Source: Company data, Goldman Sachs Research estimates.

terms of a potential tax. However, visibility remains poor and, if fully executed, price hikes to pass through the tax impact would also take time, in our view.

We revise up earnings by 19% for 2018E to reflect lower minorities, tax benefits in 1H18 and lower unit cost from NPM, although this is partly offset by our lower cobalt price assumption of US\$75,908 (YTD average, prior US\$80,012/t) and the DRC royalty tax (effective from mid June 2018); we revise down 2019E earnings by 2% to reflect a lower cobalt price assumption of US\$63,806/t (using the spot price, prior US\$80,012), partly offset by lower unit cost from NPM. Our new 12m target prices are HK\$3.7/sh (from HK\$5.6) and Rmb 5.6/sh (from Rmb 6.7). We maintain a Neutral rating on Moly-H and we upgrade Moly-A to Neutral (from Sell). Our target price methodology remains unchanged, based on historical P/B vs. ROE correlation. However, we now incorporate the potential DRC super tax impact into our valuation by applying an average of the potential best case (no super tax impact: 2019E PB of 2.0x/3.2x (H/A) and ROE at 11%) and the potential worst case (super tax fully executed as proposed: 2019E PB of 1.2x/2.4x and ROE at 7%). Over the past 2 months, Moly-A has underperformed Moly-H by around 14%, and we now view the current valuation as fair; as such, we upgrade to Neutral from Sell. Moly-A has declined by 29% YTD vs. CSI300 declined by 15%. Since being added to the Sell List on November 19, 2017, Moly-A is down 17.5% vs. the CSI300 down 17.5%.

Key risks include: 1) metal prices, including molybdenum, tungsten, copper and cobalt, 2) declining of/improving grade for mines, 3) geopolitical risk and policy risk change in DRC where the company has major assets like tax rate change.

Exhibit 1: Key items comparison between 2019 base case (no super tax charged) and with super tax

Key assumptions for DRC Tenke		Without super tax	With super tax
Metal price assumption in feasibility study			
Copper	US\$/lb	2.00	2.00
Cobalt	US\$/t	22,050	22,050
Price base for super tax (25% increase to price assumption)			
Copper	US\$/lb	2.50	2.50
Cobalt	US\$/t	27,563	27,563
2019E metal prices assumption - GSe			
Copper	US\$/lb	3.51	3.51
Cobalt	US\$/t	63,806	63,806
Price increase subject to 50% super tax			
Copper	US\$/lb	-	1.01
Cobalt	US\$/t	-	36,244
Sales volume Tenke - 2019E			
Copper	kt	190.0	190.0
Cobalt	kt	16.0	16.0
Revenue Tenke - 2019E			
Copper	Rmb mn	9,702	8,257
Cobalt	Rmb mn	6,942	4,970
China Moly key financial items		Without super tax	With super tax
Total revenue	Rmb mn	28,171	24,754
PBT	Rmb mn	8,865	5,672
Net profit	Rmb mn	4,751	3,008
Book value per share	Rmb/sh	2.012	1.931
ROE	%	11.1%	7.2%

Source: Company data, Goldman Sachs Global Investment Research

Exhibit 2: 1H18 results summary - China Moly

		1H18A	1H17A	YoY	1H18E	A vs E
Moly & Tungsten	Rmb mn	2,337	1,731	35%	2,092	12%
Niobium & Phosphorus related	Rmb mn	2,304	2,150	7%	2,252	2%
Copper & gold related	Rmb mn	842	839	0%	879	-4%
Copper & Cobalt related	Rmb mn	8,466	6,761	25%	7,711	10%
Others	Rmb mn	110	174	-36%	181	-39%
Gross revenue	Rmb mn	14,060	11,655	21%	13,115	7%
Business tax	Rmb mn	(417)	(143)	193%	(299)	39%
COGS	Rmb mn	(7,950)	(7,522)	6%	(7,348)	8%
Gross profit	Rmb mn	5,692	3,991	43%	5,580	2%
Other income	Rmb mn	72	24	200%	46	55%
Sales & dist cost	Rmb mn	(87)	(101)	-14%	(99)	-13%
Admin	Rmb mn	(530)	(463)	14%	(504)	5%
Fair value chgs	Rmb mn	(79)	(326)	-76%	-	n.a
Impairment loss	Rmb mn	(13)	(10)	26%	-	n.a
EBIT	Rmb mn	5,055	3,114	62%	5,024	1%
Share of associate/JV	Rmb mn	51	22	135%	15	239%
Finance cost, net	Rmb mn	(435)	(1,026)	-58%	(482)	-10%
Other non operating income	Rmb mn	(46)	(19)	141%	-	n.a
Income tax expenses	Rmb mn	(1,023)	(721)	42%	(1,512)	-32%
Minorities	Rmb mn	(478)	(534)	-10%	(608)	-21%
Net profit	Rmb mn	3,123	835	274%	2,436	28%
One-offs	Rmb mn	(49)	(336)	-86%	-	n.a
NP-recurring	Rmb mn	3,160	1,055	199%	2,436	30%
EPS	Rmb/sh	0.145	0.049	192%	0.113	28%
EPS-recurring	Rmb/sh	0.146	0.062	134%	0.113	30%
Gross profit		5,692	3,991	43%	5,580	2%
Moly & Tungsten	Rmb mn	1,371	832	65%	1,150	19%
Niobium & Phosphorus related	Rmb mn	476	416	14%	395	20%
Copper & gold related	Rmb mn	334	264	26%	317	5%
Copper & Cobalt related	Rmb mn	3,961	2,565	54%	3,839	3%
Others	Rmb mn	(449)	(86)	424%	(121)	270%
Prod volume						
Moly (100%)	kt	8	8	-2%	7	12%
Tungsten (100%)	kt	6	6	1%	6	-10%
Copper	kt	101	128	-21%	116	-13%
NPM	kt	17	19	-12%	17	-2%
Tenke	kt	84	109	-23%	99	-15%
Cobalt	kt	9	7	23%	8	8%
LME-copper	US\$/lb	3.16	2.61	21%	3.46	-9%
LME-cobalt	US\$/t	84,599	49,874	70%	80,012	6%
Unit COGS per copper (excl credit) - Tenke	Rmb/t	53,489	38,432	39%	39,212	36%
Unit COGS per copper (excl credit) - NPM	Rmb/t	30,503	30,373	0%	32,939	-7%
Operating cash flow	Rmb mn	5,412	3,481	55%		
Investing cash flow	Rmb mn	(3,936)	587	n.a		
Free cash flow	Rmb mn	1,476	4,069	-64%		
A/R days	days	51	45	13%		
A/P days	days	14	20	-33%		
Inv days	days	136	124	9%		
Net debt	Rmb mn	3,975	3,784	5%		
Net gearing	%	10%	10%	0%		

Source: Company data, Goldman Sachs Global Investment Research

Exhibit 3: Key assumptions and financials - China Moly

Key assumptions and financials - CMO		2015A	2016A	2017A	2018E	2019E	2020E
Moly conc-China (45%)	Rmb/t	42,537	40,444	54,287	76,218	71,020	72,521
Tungsten-WO3	Rmb/t	74,370	69,398	90,443	90,443	90,443	90,443
Cobalt	US\$/t	28,475	25,444	55,742	75,908	63,806	63,806
Copper-LME	US\$/lb	2.51	2.20	2.90	3.10	3.51	3.49
Gold	US\$/oz	1,160	1,247	1,259	1,340	1,450	1,525
Production volume							
Moly (100%)	kt	17.00	16.30	16.72	14.90	14.90	14.90
Tungsten (100%)	kt	9.83	10.12	11.74	12.00	12.00	12.00
Prod - Cobalt Tenke	kt	-	2	16	18	16	16
Prod - Cu Tenke	kt	-	23	214	190	190	190
Prod - Cu NPM	kt	40	37	35	32	29	26
Prod - Gold NPM	koz	36	29	25	28	25	23
Unit COGS-NPM	Rmb/t	23,301	27,583	32,818	33,754	35,442	36,328
Unit COGS-Tenke	Rmb/t	-	43,226	38,824	46,588	46,588	46,588
Unit cash cost-Moly	Rmb/t	53,906	55,279	54,368	63,150	63,150	63,150
Revenue	Rmb mn	4,197	6,950	24,148	28,316	28,171	28,003
EBIT recurring	Rmb mn	1,026	1,470	7,203	9,683	9,489	9,416
EBITDA recurring	Rmb mn	1,771	2,630	11,834	13,993	13,713	13,341
Net Profit	Rmb mn	761	998	2,728	5,474	4,751	4,872
EPS	Rmb/sh	0.048	0.059	0.143	0.253	0.220	0.226
BV	Rmb/sh	1.084	1.110	2.003	1.944	2.012	2.105
Net debt	Rmb mn	(599)	24,846	3,784	(2,825)	(8,727)	(14,924)
Minorities	Rmb mn	463	15,599	7,752	8,591	9,779	10,997
Operating cash flow	Rmb mn	1,359	2,915	8,429	11,250	10,196	10,056
Investing cash flow	Rmb mn	(166)	(27,648)	(4,109)	(3,000)	(1,000)	(1,000)
Free cash flow	Rmb mn	1,193	(24,733)	4,320	8,250	9,196	9,056
ROE	%	4.8%	5.5%	9.6%	13.7%	11.1%	11.0%
ROIC	%	3.0%	2.0%	6.2%	9.1%	8.3%	8.6%
Gearing(net debt/equity)	%	-3%	133%	10%	-7%	-20%	-33%
GP breakdown							
Moly&Tungsten	Rmb mn	938	1,304	1,953	2,558	2,329	2,395
Niobium&Phosphorus relate	Rmb mn	-	249	791	791	791	791
Copper & gold related	Rmb mn	512	368	518	580	726	636
Copper & Cobalt related	Rmb mn	-	300	5,542	8,468	8,464	8,400
Others	Rmb mn	125	105	131	(104)	(104)	(104)
Business tax	Rmb mn	(242)	(230)	(344)	(1,016)	(1,176)	(1,171)

Source: Company data, Goldman Sachs Global Investment Research

Disclosure Appendix

Reg AC

We, Joy Zhang and Trina Chen, hereby certify that all of the views expressed in this report accurately reflect our personal views about the subject company or companies and its or their securities. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

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GS Factor Profile

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Growth is based on a stock's forward-looking sales growth, EBITDA growth and EPS growth (for financial stocks, only EPS and sales growth), with a higher percentile indicating a higher growth company. **Financial Returns** is based on a stock's forward-looking ROE, ROCE and CROCI (for financial stocks, only ROE), with a higher percentile indicating a company with higher financial returns. **Multiple** is based on a stock's forward-looking P/E, P/B, price/dividend (P/D), EV/EBITDA, EV/FCF and EV/Debt Adjusted Cash Flow (DACF) (for financial stocks, only P/E, P/B and P/D), with a higher percentile indicating a stock trading at a higher multiple. The **Integrated** percentile is calculated as the average of the Growth percentile, Financial Returns percentile and (100% - Multiple percentile).

Financial Returns and Multiple use the Goldman Sachs analyst forecasts at the fiscal year-end at least three quarters in the future. Growth uses inputs for the fiscal year at least seven quarters in the future compared with the year at least three quarters in the future (on a per-share basis for all metrics).

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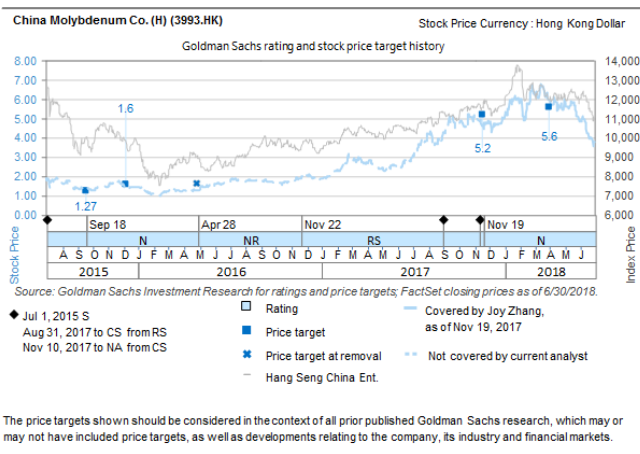
	Buy	Hold	Sell
Global	35%	53%	12%

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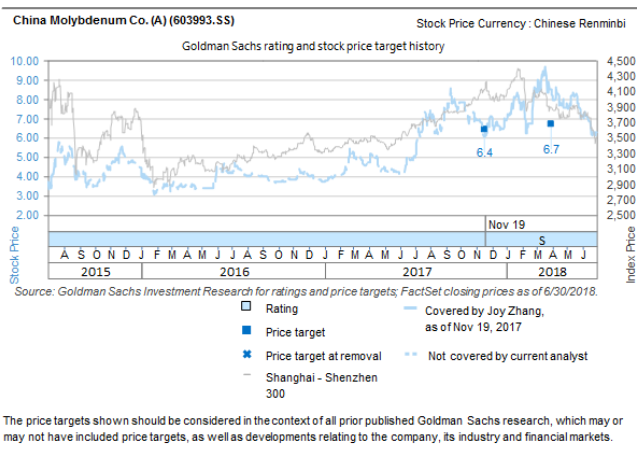
	Buy	Hold	Sell
	63%	56%	51%

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