

China

REDUCE

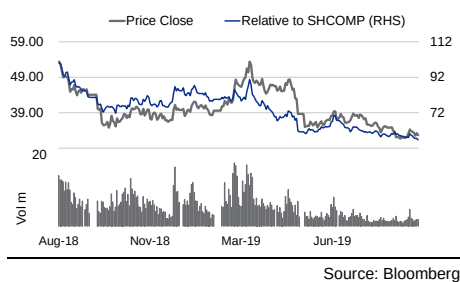
Consensus ratings*: Buy 3 Hold 2 Sell 3

Current price:	Rmb32.68
Target price:	Rmb14.24
Previous target:	Rmb19.41
Up/downside:	-56.4%
CGS-CIMB / Consensus:	-57.7%
Reuters:	601869.SS
Bloomberg:	601869 CH
Market cap:	US\$2,388m
	Rmb17,101m
Average daily turnover:	US\$12.33m
	Rmb85.44m
Current shares o/s:	757.9m
Free float:	32.7%

*Source: Bloomberg

Key changes in this note

- FY19F and FY20F net profit decreased by 3.2% and 8.1%, respectively..



Price performance	1M	3M	12M
Absolute (%)	-6.7	-11.4	-37.3
Relative (%)	-5	-10.8	-41.5

Major shareholders	% held
China Huaxin	23.7
Draka	23.7

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YOFC-A

Weak 1H 2019 results; no major recovery signs

- YOFC-A reported its 1H 2019 results; core operating performance was still weak, given soft end demand and an unfavourable product mix.
- During the results presentation, management guided that 2019 has been a challenging period for the whole industry.
- Management remains positive on the outlook, given the 5G roll-out, and mentioned that co-building and co-sharing may ease pressure on the financial position of telecom operators.
- We revised downward our net profit forecast for YOFC-A in 2019 and 2020 after the weak 1H 2019 results.
- YOFC-A's current valuation is not particularly expensive, but we don't see any major re-rating catalysts. We cut our target price further from RMB19.41 to RMB14.24 because of a 3.2% cut in our 2019F earnings forecasts, recent weakness in the RMB, and 8x PER for YOFC-H (vs. our previous target PER of 10x). Our target price for YOFC-A is based on 30%% premium to our YOFC-H target price.

Weak 1H 2019 results

YOFC-A reported a 41% YoY decline in turnover and 46% YoY decline in net profit in 1H 2019, which implies that turnover and net profit dropped 45.7% YoY and 58.0% YoY, respectively, in Q2 2019. Q2 was a challenging period for the industry, given soft end demand. YOFC-A's gross profit margin in 1H 2019 dropped 4.7ppts to 23.5% (Q1 2019: 26.9%; Q2 2019: 19.7%). According to YOFC-A management, the drop in gross profit margin in 1H 2019 was due to an unfavourable product mix, as the Company intended to hold sales of preform and wait for better pricing going forward. We should see better Q3 and Q4 2019 results, as China Mobile kicked off delivery of optical cable in late Q2 2019. China Telecom is expected to kick off delivery of optical cable in 2H 2019. Management expects sales of preform to pick up in 2H vs. 1H 2019, as shipments of optical cable to two operators started. YOFC-A management mentioned that the Company's bidding price for products to China Telecom was about 12.5% higher than the products to China Mobile. Management believes that this is a sign of stabilization and that it is not a surprise that some investors might treat this as a catalyst for the optical fibre cable supply chain, including YOFC-A. However, we don't think it is a sign of recovery, as there are over 20 players on China Telecom's supplier list, and the bidding price still dropped YoY. It is unlikely that the ASP of optical cable will move up further in Sep-Dec 2019.

No bottom fishing yet in the short term

YOFC-A management remains positive on the outlook for the Company, given the 5G roll-out and believes demand for optical cable products will pick up after installation of wireless equipment in 2020. Co-building and co-sharing are expected ease financial pressure on the telecom operators, especially China Telecom and China Unicom, which may result in the roll-out process speeding up in early stage. In the long term, YOFC-A's growth will be supported by new product development, such as ULL optical fibre, which is expected to be used to upgrade the main trunk of the optical fibre network of Chinese telecom operators. However, we suggest investors wait for confirmation of demand pick-up before re-rating YOFC-A. We still believe that the optical cable supply chain will be later-cycle names under the 5G theme.

Downward earnings revision

We cut our turnover forecast for 2019F by 16.8% and for 2020F by 18.9%, after the 1H 2019 results revision. We also cut our 2018F and 2019F net profit forecasts by 3.2% and 8.1%, respectively, due to downward revision of the turnover forecasts. Our gross margin forecasts for 2019F and 2020F are also cut by 0.32ppt and 0.18ppt, respectively.

Financial Summary	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Revenue (Rmbm)	10,366	11,360	7,899	8,759	9,877
Operating EBITDA (Rmbm)	1,626	1,819	1,160	1,359	1,560
Net Profit (Rmbm)	1,268	1,484	975	1,008	1,155
Core EPS (Rmb)	1.86	2.06	1.29	1.33	1.52
Core EPS Growth	76.9%	10.8%	(37.6%)	3.4%	14.6%
FD Core P/E (x)	17.58	15.86	25.40	24.58	21.44
DPS (Rmb)	0.00	0.75	0.39	0.40	0.46
Dividend Yield	0.00%	2.29%	1.18%	1.22%	1.40%
EV/EBITDA (x)	13.51	12.60	21.03	18.41	15.98
P/FCFE (x)	62.36	NA	93.11	NA	33.00
Net Gearing	(10.4%)	(9.6%)	(6.4%)	0.6%	(0.3%)
P/BV (x)	4.26	3.02	2.88	2.87	2.61
ROE	27.0%	22.1%	11.6%	11.7%	12.8%
% Change In Core EPS Estimates					
CIMB/consensus EPS (x)			0.96	0.81	0.80

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

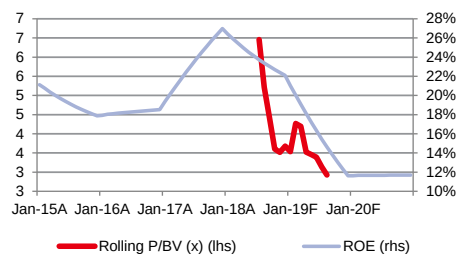
Figure 1: Assumptions

	2013	2014	2015	2016	2017	2018	2019F	2020F	2021F
Turnover (RMBm)									
Optical fibre preforms and fibres	2,722.7	3,229.7	3,756.6	4,073.1	4,702.9	4,691.2	3,668.0	4,236.6	4,893.2
Optical fibre cables	1,817.6	1,989.4	2,643.3	3,580.7	5,034.9	5,726.7	3,430.5	3,602.0	3,971.2
Other products and services	285.6	457.7	331.3	457.7	628.2	941.8	800.5	920.6	1,012.7
Total	4,825.9	5,676.8	6,731.1	8,111.5	10,366.1	11,359.8	7,899.1	8,759.2	9,877.1
YoY Change (%)									
Optical fibre preforms and fibres		18.6	16.3	8.4	15.5	(0.2)	(21.8)	15.5	15.5
Optical fibre cables		9.5	32.9	35.5	40.6	13.7	(40.1)	5.0	10.3
Other products and services				38.2	37.3	49.9	(15.0)	15.0	10.0
Total		17.6	18.6	20.5	27.8	9.6	(30.5)	10.9	12.8
Gross margin (%)	21.1	19.2	19.4	20.3	26.3	27.9	25.4	26.0	26.2
Optical fibre preforms and fibres	27.3	25.3	26.0	27.6	36.7	40.6	36.0	36.0	36.0
Optical fibre cables	11.7	9.1	8.5	10.0	16.0	17.9	13.0	13.0	13.0
Other products and services	21.4	19.4	30.8	53.7	40.5	45.3	53.9	53.9	53.9
Net margin (%)	8.6	8.2	8.5	8.8	12.2	13.1	12.3	11.5	11.7
YoY Change (%)									
ASP									
Optical fibre preforms		(7.9)	0	4.0	16.2	0	(15.0)	5.0	5.0
Optical fibres		(6.7)	5.0	3.5	0	(0.4)	(10.0)	5.0	5.0
Optical fibre cables		(1.3)	(5.1)	8.4	18.0	3.0	(30.0)	0	5.0
YoY Change (%)									
Volume									
Optical fibre preforms		33.8	20.0	7.0	0	0	(5.0)	10.0	10.0
Optical fibres		24.5	8.7	3.0	15.0	0	(15.0)	10.0	10.0
Optical fibre cables		10.9	40.0	25.0	19.2	5.0	(10.0)	5.0	5.0
Cost (HKDm)									
S,G&A	(548.6)	(565.4)	(714.4)	(861.7)	(1,273.0)	(1,549.0)	(1,124.5)	(1,229.4)	(1,386.3)
Financial Expenses	(68.0)	(78.0)	(81.3)	(99.2)	(156.4)	(112.2)	(78.2)	(87.6)	(95.9)
YoY Change (%)									
S,G&A		3.1	26.4	20.6	47.7	21.7	(27.4)	9.3	12.8
Financial Expenses		14.8	4.2	22.1	57.6	(28.2)	(30.3)	12.0	9.6
CAPEX (RMBm)	n.a.	n.a.	112.4	278.5	161.5	233.8	1,100.0	600.0	690.0

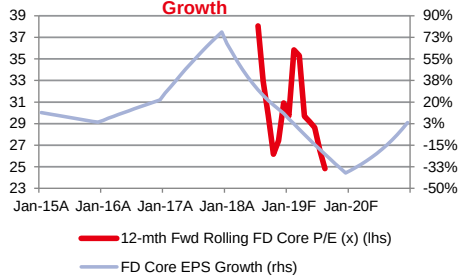
SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

BY THE NUMBERS

P/BV vs ROE



12-mth Fwd FD Core P/E vs FD Core EPS Growth



Profit & Loss

(Rmbm)	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Total Net Revenues	10,366	11,360	7,899	8,759	9,877
Gross Profit	2,899	3,368	2,285	2,588	2,946
Operating EBITDA	1,626	1,819	1,160	1,359	1,560
Depreciation And Amortisation	(173)	(201)	(274)	(314)	(360)
Operating EBIT	1,453	1,618	886	1,044	1,200
Financial Income/(Expense)	(63)	(60)	(70)	(79)	(80)
Pretax Income/(Loss) from Assoc.	159	152	122	146	153
Non-Operating Income/(Expense)	(101)	(46)	154	13	18
Profit Before Tax (pre-EI)	1,447	1,664	1,091	1,124	1,291
Exceptional Items					
Pre-tax Profit	1,447	1,664	1,091	1,124	1,291
Taxation	(212)	(181)	(116)	(117)	(136)
Exceptional Income - post-tax					
Profit After Tax	1,235	1,482	974	1,007	1,154
Minority Interests	34	1	1	1	1
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	1,268	1,484	975	1,008	1,155
Recurring Net Profit	1,268	1,484	975	1,008	1,155
Fully Diluted Recurring Net Profit	1,268	1,484	975	1,008	1,155

Cash Flow

(Rmbm)	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
EBITDA	1,626	1,819	1,160	1,359	1,560
Cash Flow from Inv. & Assoc.					
Change In Working Capital	(151)	(998)	352	(248)	(323)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	263	209	360	211	212
Net Interest (Paid)/Received	(63)	(60)	(70)	(79)	(80)
Tax Paid					
Cashflow From Operations	1,674	970	1,801	1,242	1,369
Capex	(161)	(234)	(1,100)	(600)	(690)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments	(546)	(688)	0	0	0
Other Investing Cashflow	165	(608)	(351)	(670)	44
Cash Flow From Investing	(542)	(1,530)	(1,451)	(1,270)	(646)
Debt Raised/(repaid)	(774)	370	(84)	21	27
Proceeds From Issue Of Shares	0	1,905	0	0	0
Shares Repurchased					
Dividends Paid	(233)	(379)	(189)	(293)	(302)
Preferred Dividends					
Other Financing Cashflow	52	(461)	(298)	(301)	(349)
Cash Flow From Financing	(956)	1,435	(571)	(572)	(625)
Total Cash Generated	176	875	(221)	(599)	99
Free Cashflow To Equity	357	(190)	266	(6)	750
Free Cashflow To Firm	1,210	(472)	446	71	824

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

BY THE NUMBERS... cont'd

Balance Sheet

(Rmbm)	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Total Cash And Equivalents	1,800	2,684	2,463	1,864	1,962
Total Debtors	2,535	3,553	2,812	3,119	3,517
Inventories	805	1,088	865	959	1,082
Total Other Current Assets	89	163	124	133	146
Total Current Assets	5,229	7,488	6,264	6,075	6,707
Fixed Assets	1,922	2,017	2,843	3,128	3,458
Total Investments	0	0	0	0	0
Intangible Assets	0	0	0	0	0
Total Other Non-Current Assets	2,017	3,381	3,535	3,697	3,866
Total Non-current Assets	3,939	5,398	6,378	6,825	7,324
Short-term Debt	748	1,066	1,082	1,101	1,121
Current Portion of Long-Term Debt					
Total Creditors	1,705	2,008	1,396	1,548	1,746
Other Current Liabilities	495	277	192	213	241
Total Current Liabilities	2,948	3,350	2,671	2,862	3,107
Total Long-term Debt	481	817	817	817	817
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	170	263	284	306	331
Total Non-current Liabilities	651	1,080	1,101	1,123	1,148
Total Provisions	83	80	88	97	106
Total Liabilities	3,682	4,510	3,859	4,082	4,361
Shareholders' Equity	5,238	8,188	8,595	8,631	9,484
Minority Interests	248	188	188	187	186
Total Equity	5,486	8,376	8,782	8,818	9,670

Key Ratios

	Dec-17A	Dec-18A	Dec-19F	Dec-20F	Dec-21F
Revenue Growth	27.8%	9.6%	(30.5%)	10.9%	12.8%
Operating EBITDA Growth	77.5%	11.9%	(36.2%)	17.1%	14.8%
Operating EBITDA Margin	15.7%	16.0%	14.7%	15.5%	15.8%
Net Cash Per Share (Rmb)	0.84	1.06	0.74	(0.07)	0.03
BVPS (Rmb)	7.68	10.80	11.34	11.39	12.51
Gross Interest Cover	18.58	18.48	9.23	10.66	11.93
Effective Tax Rate	14.7%	10.9%	10.7%	10.4%	10.6%
Net Dividend Payout Ratio	NA	38.3%	30.0%	30.0%	30.0%
Accounts Receivables Days	82.8	97.8	147.1	123.9	122.6
Inventory Days	36.63	43.23	63.47	54.10	53.74
Accounts Payables Days	75.3	84.8	110.6	87.3	86.7
ROIC (%)	34.1%	31.3%	11.2%	12.2%	12.9%
ROCE (%)	23.4%	19.2%	8.6%	9.8%	10.8%
Return On Average Assets	15.0%	14.0%	8.2%	8.5%	9.2%

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

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We are transferring the rating mechanism from "BUY, SELL, HOLD" to "ADD, REDUCE, HOLD". Please refer to the definitions below.

Explanation on Equity Ratings (Existing mechanism (will be replaced by new mechanism by 01/09/19))

BUY : share price will increase by >20% within 12 months in absolute terms

SELL : share price will decrease by >20% within 12 months in absolute terms

HOLD : no clear catalyst, and downgraded from BUY pending clearer signal to reinstate BUY or further downgrade to outright SELL

Explanation on Equity Ratings (New mechanism)

ADD : The stock's total return is expected to exceed 10% over the next 12 months.

REDUCE : The stock's total return is expected to fall below 0% or more over the next 12 months.

HOLD : The stock's total return is expected to be between 0% and positive 10% over the next 12 months.

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