

Analyst: Sam Ho

## **Main Board H-share Listing- Research**

福建紫金礦業股份有限公司

Fujian Zijin Mining Industry Co., Ltd. [Stock Code: 2899]

**Sponsor, Global Coordinator, Bookrunner and Lead Manager** : China Everbright Capital

**Sector** : Mining

**Business** : Exploration, mining, production, refining as well as sale of gold and copper in the PRC

**Total share offer:** **348,300,000 shares**  
(27.50% of the enlarged share capital)

**Placement:** 313,470,000 shares (90%)  
-281,806,364 new H shares  
-31,663,636 sale H shares

**IPO:** 34,830,000 shares (10%)

**Greenshoe:** 52,245,000 shares

**Price:** HK\$2.90-HK\$3.30 per share  
**H-share market cap. :**  
HK\$1,010.07 million-HK\$1,149.39 million

**Prospective FY2003 P/E:**  
13.4x-15.2x (fully diluted)  
**Adjusted NAV per share:** HK\$1.022

**Staffing:** 1,016

**Book opens:** 3<sup>rd</sup> December 2003  
**Book closes:** 12<sup>th</sup> December 2003

**IPO opens:** 11<sup>th</sup> December 2003  
**IPO closes:** 16<sup>th</sup> December 2003

**Share registrar:** Computershare Hong Kong  
Investor Services Limited

**Receiving bank:** Bank of China (Hong Kong)

**Listing date:** 23<sup>rd</sup> December 2003

### **Business of Fujian Zijin Mining Industry**

The Company is principally engaged in the exploration, mining, production, refining as well as sale of gold and other mineral resources in the PRC.

The Company currently operates open-cut gold mines at Zijinshan in Fujian province and Paodaoling in Anhui province, both of which use the heap leach processing method. It also runs the Hunchun Gold-copper Mine in Jilin province. In addition, Shuiyindong, Jiaochong and Caodi gold projects are expected to begin operating in 2003-2005. Furthermore, a feasibility study is currently carried out on an underground copper mine at Zijinshan, while the Asele copper-zinc project in Xinjiang Uygur autonomous region is under construction. Both copper projects are expected to commence operations before the end of 2004.

Zijinshan Gold Mine, the Company's major operating asset, is home to the country's single-largest gold deposit, amounting to 4%-5% of China's annual gold output. It is estimated to hold total gold reserves of 138.4 tonnes, according to the Ministry of Land and Resources. The Company's mining right of this gold mine will expire in 2018.

### **Major Shareholders after Listing**

*(Assuming the over-allotment option is not exercised)*

|                                    |               |
|------------------------------------|---------------|
| Xinghang Investment (Note 1)       | 33.61%        |
| Xinhuadu Industrial                | 16.33%        |
| Jinshan Trading                    | 13.51%        |
| Xiamen Hangxing (Note 2)           | 6.32%         |
| Fujian Gold Group (Note 1)         | 1.20%         |
| Xinhuadu Department Store (Note 3) | 1.29%         |
| Minxi Geologist (Note 1)           | 0.24%         |
|                                    | <u>72.50%</u> |

**Note 1: State-owned enterprises**
**Note 2:** Xiamen Hangxing is 73.21% owned by Ke Xiping, a non-executive director of the Company

**Note 3:** Xinhuadu Department Store is 64.54% owned by Xinhuadu Industrial

*This report has been prepared solely for information purposes and we are not soliciting any action based upon it. Neither this document nor its contents shall be construed as an offer, invitation, advertisement, inducement or representation of any kind or form whatsoever. The information is based upon information, which we consider reliable, but accuracy or completeness is not guaranteed. Opinions expressed herein are subject to change without notice. At time of this report, East Asia Securities Company Limited has no position in securities of the Company or companies mentioned herein.*

### Use of Proceeds

Net proceeds from the offer are estimated to be HK\$934.0 million (Based on the mid-point of the price range of HK\$3.10 each and assuming the over-allotment option is not exercised)

|   | HK\$ million |
|---|--------------|
| To be used for the combined utilization of the gold-containing solid tailings and environmental management of the Zijinshan Gold Mine     | 160.8        |
| To seek opportunities to acquire additional gold resources in the central and western parts of the PRC and prospecting for gold resources | 142.9        |
| To use for the capital contribution to the Company's subsidiaries   | 95.2         |
| To develop the Zijinshan Copper Mine  | 81.0         |
| To acquire the mining and exploration rights of mines in the peripheral zones of Zijinshan Gold Mine                                      | 76.2         |
| To serve as general working capital   | Balance      |

### Financial Highlights

|                            | 6 months ended<br>30 <sup>th</sup> June 2003<br>RMB '000 | 2002<br>RMB '000 | Year ended 31 <sup>st</sup> December<br>2001<br>RMB '000 | 2000<br>RMB '000 |
|----------------------------|--|------------------|--|------------------|
| Revenue                    |  |                  |  |                  |
| Gold                       | 485,257  | 584,232          | 325,726  | 289,650          |
| Gold material              | 4,327  | -                | 46,780   | 8,362            |
| Copper and iron            | 14,002   | 13,067           | -  | -                |
| Less: sales taxes & levies | (3,452)  | (4,645)          | (2,749)  | (1,915)          |
|                            | <u>500,134</u>   | <u>592,654</u>   | <u>369,757</u>   | <u>296,097</u>   |
| Operating profit           | <u>231,010</u>   | <u>220,736</u>   | <u>110,064</u>   | <u>83,881</u>    |
| Net profit                 | <u>154,117</u>   | <u>138,283</u>   | <u>66,102</u>  | <u>48,427</u>    |
| EPS                        | <u>RMB1.62</u>   | <u>RMB1.46</u>   | <u>RMB0.70</u>   | <u>RMB0.73</u>   |
| Dividend                   | -  | 95,000           | 47,500   | 11,875           |

### Mineral Assets Summary

| Gold mines   | Location | Mineral resources (kg)    | Average grade (g/tonne) | Mining right expiry |
|--------------|----------|---------------------------|-------------------------|---------------------|
| Zijinshan    | Fujian   | 138,351                   | 1.20                    | July 2018           |
| Hunchun      | Jilin    | 27,504                    | 1.15                    | 2005; 2010          |
| Shuiyingdong | Guizhou  | 21,761                    | 9.57                    | June 2008           |
| Paodaoling   | Anhui    | 6,320                     | 2.10                    | May 2012            |
| Caodi        | Sichuan  | 26,422                    | 2.57                    | N/A                 |
| Jiaochong    | Anhui    | 14,824                    | 5.94                    | N/A                 |
| Copper mines | Location | Mineral resources (tonne) | Average grade (%)       | Mining right expiry |
| Zijinshan    | Fujian   | 1,465,000                 | 0.66                    | July 2018           |
| Asele        | Xinjiang | 919,454                   | 2.43                    | January 2031        |
| Hunchun      | Jilin    | 78,187                    | 0.33                    | 2005; 2010          |

### Summary of Zijinshan Gold Mine

| Mineral resources category | Tonnes             | Gold grade (g/tonne) | Contained gold quantity (kg) |
|----------------------------|--------------------|----------------------|------------------------------|
| Measured                   | 13,620,295         | 1.71                 | 23,291                       |
| Indicated                  | 56,504,190         | 1.27                 | 71,760                       |
| Indicated and inferred     | <u>45,103,937</u>  | <u>0.96</u>          | <u>43,300</u>                |
| <b>Total</b>               | <b>115,228,422</b> | <b>1.2</b>           | <b>138,351</b>               |

**Strengths**

- ✓ According to the World Gold Council, demand for gold in China for use in jewellery, industry and as gold bars accounted for 6% of the world's physical demand in 2002, and amounted to 214.3 tonnes. Given the growing consumption, industrial and investment needs, demand is expected to rise by an average 5%-8% for the next 10 years.
- ✓ The Company's prospect is highly dependent on the price of gold. The recent upsurge in international gold price (over US\$400/oz) should be favourable to the Company. Currency moves (especially weakness in US dollar) and the unattractive bond markets are the primary drives for the gold price. However, it is expected the short-term outlook of gold price would be quite volatile.
- ✓ The Company has been granted the use of the International Standardisation Product symbol and has also received the ISO 9002: 2000 certification. In addition, its gold smelter is the 1<sup>st</sup> to be recognized by the Shanghai Gold Exchange as capable of producing 1<sup>st</sup>-class gold bullion.
- ✓ The Company's gold production cost is, on average, about 25% below that of global players and about 22% below that of similar operators in China. One key reason is that its major mine, Zijinshan, is an open-pit ore operation, whereas 90% of the gold mines in China are underground, which results in higher operating costs. Going forward, the Company's gold production cost will increase as it will develop new, underground gold mines. However, it is expected that its cost is still below the average level, as it contracts out the stripping and transport processes to several 3<sup>rd</sup>-party operators, so as to reduce costs for equipment and staff training.
- ✓ The Company will develop 3 other gold mines (Shuiyindong, Jiacong and Caodi), with operations scheduled to commence between 2003 and 2005. Accordingly, its gold output is expected to increase at a CAGR of over 20% from 2003-2005. Moreover, the Company is accelerating the development of its copper reserves.
- ✓ The Company will be the 1<sup>st</sup> China play on the local bourse with exposure to the gold-mining industry.
- ✓ Fujian Zijin was priced at 2003E P/E of 13.4x-15.2x. Since there is no direct comparable available in the market, we may use other precious-metal stocks' valuations as a reference. Jiangxi Copper (*stock code: 0358*) is trading at 2003E P/E of 16.97x, while Chalco (*stock code: 2600*) is trading at 2003E P/E of 14.6x. Thus, valuation of Fujian Zijin is undemanding. In addition, international gold-mining plays are generally trading at FY2003E P/E of over 20x.

**Weaknesses**

- × The gold-mining industry in China is highly fragmented, with the largest miner (Fujian Zijin) accounting for only 2.4% market share in terms of annual production volume in 2001. With the mining industry being opened to foreign investors following China's entry to the WTO, competition for exploiting gold ore should be intensifying, especially as high-grade gold ore is relatively scarce in China.
- × Gold producers must continually replace gold reserves depleted by production. However, gold exploration is highly speculative in nature, involves many risks and is frequently unproductive. There is no assurance that new or ongoing exploration programmes will result in new mineral-producing operations. Moreover, estimates of proven and probable reserves are subject to considerable uncertainty.
- × The Shanghai Gold Exchange has not yet offered any kind of hedging instruments (such as forward or futures contracts) for local miners to lock in gold prices.

**Recommendation: Subscribe**