

Analyst: Kevin Tam

Main Board Listing (H-shares) – Research

中國建材股份有限公司 (03323)

China National Building Material Company Limited [Stock Code: 3323]

Sole Global Coordinator, Book-runner, Lead Manager and Sponsor : Morgan Stanley
Co-Lead Managers : China International Capital Corporation (Hong Kong)
Daiwa Securities SMBC

Sector : Materials

Business : Materials

Total H share offer: <u>654,214,000</u> shares (33% of the enlarged share capital) Public Offer: 65,422,000 shares (10%) Placing: 588,792,000 shares (90%) Greenshoe: 98,120,000 shares (15%)	<u>Business of China National Building Material</u> The Company is a leading PRC building materials company with significant operations in the cement, lightweight building materials, glass fibre and FRP products and engineering services business segments. In terms of 2004 market positions, the Company is (i) the largest cement producer in the Huaihai Economic Zone of the PRC; (ii) the largest gypsum board producer in the PRC, with a combined market share of approximately 50.96%; (iii) the largest glass fibre producer in Asia; (iv) one of the largest glass fibre mats producers in the PRC; (v) the second largest FRP (fibre-glass reinforced plastics) pipes and tanks producer in the PRC; (vi) the engineering firm that designed and/or constructed approximately 50% of the float glass production lines in the PRC. For the nine months ended September 2005, cement, lightweight building materials, glass fibre and FRP products and engineering services accounted for 26.7%, 50.3%, 6.7% and 17.7% of total revenue respectively.
Price: HK\$2.30 – HK\$2.75 per share H Share Market Cap.: HK\$4,560 million – HK\$5,452 million Pro Forma FY2005E P/E: 13.50x – 16.14x Adjusted NTA per share: HK\$1.56 – HK\$1.69 Group Staffing: 8,793	
HK Public Offer period: 13 th March 2006 – 16 th March 2006 Receiving bank: Bank of Communications (HK) Bank of China (HK) Share registrar: Tricor Investor Services Limited Listing date: 23 rd March 2006	

Major Shareholders after Listing (Assuming the over-allotment option is not exercised)

China National Building Material Group Corp – a state-owned enterprise & its group co. ⁽¹⁾	63.48%
China Cinda Asset Management Corporation	3.51%
	<u>66.99%</u>

⁽¹⁾ China National Building Material Group owns the Group through direct ownership (17.78%), Beijing New Building Material Group (39.6%), CNBM Trading (6.07%), and Building Material Academy (0.03%).

Use of Proceeds

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Net proceeds from the offer are estimated to be HK\$1,516 million.

(Assuming the over-allotment option is not exercised, and at an issue price of HK\$2.75 each, being the upper-point of the indicative price range)

	HK\$ million
Clinker production line for Qingzhou	350
Clinker production line for Nanyang	250
Gypsum board production line	140
Glass fibre reinforced cement board production line	150
Glass fibre mat production line for Zhongxin Tianma	50
Phase 1 of a cement grinding station for Fuyang Julong	40
Phase 1 of a cement grinding station for Suqian Julong	25
Debt repayment	>100

Financial Highlights

	Year ended 31 st December			9 months ended
	2002	2003	2004	30 th Sept., 2005
	RMB million	RMB million	RMB million	RMB million
Sales	1,661.5	1,845.2	2,898.1	3,334.4
Gross profit	371.2	418.4	554.8	601.4
Operating profit	159.8	140.3	296.5	360.1
Net profit	99.2	111.7	193.1	223.9
Shareholders' Equity	1,657.1	1,681.1	1,888.6	1,985.0

Strengths/Opportunities

- ✓ The cement industry is generally a regional industry because its heavy and bulky nature makes cross-region competition very difficult. The Company's leading position in the Huaihai Economic Zone is not easy to be challenged. Locating in southern Shangdong and northern Jiangsu, its production plant has access to some of the richest limestone deposits, the raw material of cement, in the PRC. The group is well positioned to benefit from the current consolidation in the cement industry given its leading position. Moreover, there are initial signs showing the cement industry has just passed its cyclical downturn.
- ✓ Gypsum board consumption in China is optimistic because energy and resource economical and environmental friendly products are replacing traditional wall materials. The Group has a combined share of approximately 50.6% in the industry after the Taihe acquisition.
- ✓ The production capacity of glass fibre in China has been consolidated into a few manufacturers. Glass fibre prices stayed relatively stable. China Fiberglass, of which the Group hold 40.17%, accounted for approximately 22.8% of China's national glass fiber output and 21.1% of China's glass fibre exports.
- ✓ Despite gross margin declining from 22.34% in 2002 to 18.04% in the first nine months of 2005, operating margin managed to expand from 9.62% to 10.8%. This past record demonstrates how economy of scale helped minimize operating cost despite rising raw material and energy costs.

Weaknesses/Threats

- × The cement segment, accounting for 26.7% of total sales or 38.6% of total operating profit, is heavily exposed on energy cost. Fuel and power costs accounted for approximately 53.2%, 47.5%, 56.4% and 61.8% of total cement sales in 2002 to 2004, and the nine months of 2005, respectively.
- × The Group is highly leveraged. For the nine months ended September 2005, the fixed charge coverage ratio is just 4.12X. At September 30, total debt was RMB 4,185 million, of which 3,011 million would be due within one year. Debt to equity ratio before the IPO is 129%, even the estimated post IPO debt to equity ratio is still at a high of 85.4%.
- × The operation of the Group is capital intensive. For the year 2002 to 2004, and the first nine months of 2005, capital expenditure amounted to RMB 222 million, RMB 229 million, RMB 1,535 million and RMB 931 million respectively, offsetting almost all the operating cash flow of the respective year.

Recommendation: Trading Buy

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