

China | Alert

16 December 2014

Zhaojin Mining Industry

Bolt-on acquisition for long-term growth

IN-LINE

PRICE (as of 15 Dec 2014)	BLOOMBERG	REUTERS	12 MONTH RANGE	MARKET CAP
HKD 4.04	1818 HK	1818.HK	HKD 3.80 - 5.73	HKD 11,982mn (USD 1,545mn)

- On 15 December, Zhaojin Mining announced that it will acquire a 51% stake in Binghua Mining, whose principal asset is the mining rights to a gold mine in Xiahe County in the south of Gansu province, which is a prospective gold belt.
- The purchase price of RMB 15mn per tonne of gold resource is lower than RMB 17mn per tonne in recent transactions.
- The estimated gold resource of the mine ranges from 100-120t, which would add c.13-15% to the company's gold resources, based on the company's FY13 disclosure. Earnings contribution would be negligible, as the mine generated net profit of only RMB 4mn in 2013, according to the announcement.
- We believe this deal will add to the company's long-term growth potential; however, financial costs could increase in the short term, and production costs and the quality of gold resources are not clear at this stage. We maintain our IL rating and a price target of HKD 4.57.

Details of the acquisition

On 15 December 2014, Zhaojin Mining announced that it has entered into an equity transfer agreement with Xinxiang Company, Lin Jinfang, Chen Tiande and Hong Zhenchao to acquire a 51% interest in Binghua Mining (the target company), whose principal asset is the mining rights to a gold mine located in Jiagantan, Xiahe County, at a unit price of RMB 15mn per tonne. Boyan Mining will acquire a 29% stake and the total 80% equity interest will be transferred at one go.

Zhaojin will pay RMB 288mn, based on current estimated gold reserves of 40t (50% within five working days after entering into the agreement and 50% within five working days after the completion of the ownership change). The final consideration will be determined based on mineral reserves, reported by an independent third party after completing exploration on 31 December 2014. The unit price is set at RMB 15mn per tonne.

According to Zhaojin's own examination, total gold reserves of the gold mine range from 100-120t (higher than the current estimate of 40t), which would cost the company RMB 747mn-900mn for the 51% stake. Zhaojin will make further announcements if the final consideration paid by the company is more than RMB 900mn. Additionally, the company agreed to pay another RMB 19mn to increase capital on the mine within five working days after the completion of the ownership change.

The unit price of RMB15mn per tonne is about 11% lower than RMB 17mn per tonne in recent transactions, although we note that M&A in the gold mining space has been inactive recently. We believe Zhaojin has a good chance to exceed expectations on its 2014 reserve addition target (50t) through the acquisition, and the final consideration for the transaction is likely to exceed the company's 2014 investment plan for new gold reserves (RMB 150mn).

Binghua Mining's 2013 net profit was RMB 4mn, representing less than 1% of Zhaojin's 2013 net profit.

We maintain our In-Line rating with a price target of HKD 4.57.

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Important disclosures can be found in the Disclosures Appendix

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Date	Recommendation	Price target	Date	Recommendation	Price target	Date	Recommendation	Price target
1 26 Mar 12	OUTPERFORM	23.59	4 26 Mar 13	OUTPERFORM	18.33	7 28 Jan 14	UNDERPERFORM	4.00
2 11 Aug 12	OUTPERFORM	13.10	5 20 Apr 13	OUTPERFORM	11.54	8 26 Mar 14	UNDERPERFORM	4.16
3 6 Oct 12	OUTPERFORM	19.53	6 23 Jul 13	IN-LINE	5.43	9 20 Aug 14	IN-LINE	4.57

Source: FactSet prices, SCB recommendations and price targets

Recommendation Distribution and Investment Banking Relationships

	% of covered companies currently assigned this rating	% of companies assigned this rating with which SCB has provided investment banking services over the past 12 months
OUTPERFORM	55.6%	10.8%
IN-LINE	33.6%	9.4%
UNDERPERFORM	10.8%	9.7%

As of 30 September 2014

Research Recommendation

Terminology	Definitions
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