



BUY

Close	Target
HK\$2.21	HK\$3.20

China / Utilities

30 September 2009

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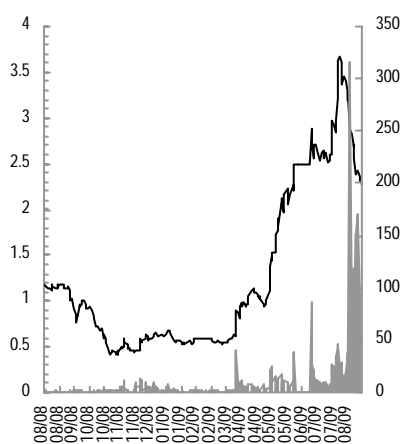
Key stock data

12-month High / Low	HK\$3.84/0.365
1m avg daily vol	43.9m
Issued shares	12,363m
Market cap	HK\$27,322m
PEG 09-11F (x)	0.3
P/E FY09F (x)	14.5
Net gearing 08A (%)	108
Board lot	1,000
Major shareholder	Zhu Gong Shan (50.26%)

Source: Bloomberg

Performance	1 M	3 M	12M
Absolute (%)	1.84	-15.65	142.86
Rel (HSI) (%)	-4.69	-29.98	126.22

Source: Bloomberg



GCL-Poly Energy (3800 HK)

Solar ramp up on track

GCL-Poly Energy Holdings (GCL-Poly) (3800 HK) reported a sturdy 1H09 net profit growth of 250% yoy to RMB71.9mn on higher power tariff and lower coal fuel cost. Besides the power operation, polysilicon operation will start to contribute most of the earnings in 2H09 after the completion of acquisition at the end of July. Production ramp-up and polysilicon delivery are on track but we marginally lower our FY09-11 EPS forecasts due to lower ASP and sales volume of polysilicon. Thus, TP is down to HK\$3.2 from HK\$3.54 but maintain **BUY**.

- ◆ **Stunning 1H09 EPS growth on strong power operation.** GCL-Poly's 1H09 net profit jumped 250% yoy to RMB71.9mn. The increase in on-grid tariffs in July and August 2008, the drop in spot coal price and the decrease in banks' interest rate were the earnings drivers for 1H09.
- ◆ **Slump in 1H09 polysilicon profit margin.** In the face of polysilicon price crash in 4Q08, GCL-Poly suffered substantial gross margin contraction in 1H09. 1H09 GPM of polysilicon segment plunged to 41.4%, compared with 72.6% in FY08.
- ◆ **Power business will remain strong momentum in 2H09.** We expect GCL-Poly's power business to improve further in 2H09 as power demand growth in the country has returned to positive territory since June 2009 and this should help improve GCL-Poly's utilization rate. Stable spot coal prices and low interest rate should help mitigate the cost pressure in 2H09. Nevertheless, polysilicon business will eclipse power business in 2H09 as the main profit center.
- ◆ **The worst for polysilicon is over.** Polysilicon volume sales will explode hoh in 2H09 as the production target of 7,500 for FY09 is on track. Given the stabilized spot price and lower production cost, we expect GPM of polysilicon business to substantially improve to 44.4% in 2H09 from 41.4% in 1H09.
- ◆ **Lower TP to HK\$3.2 on lower profit from polysilicon. Maintain BUY.** We have lowered our FY09-11 EPS forecasts by 7%, 5% and 4% respectively as we marginally lower our polysilicon ASP and shipment assumptions. Our revised TP of HK\$3.2 represents FY10F PBR of 2.7x and PER of 14.0x. Maintain **BUY**.

Key Financials

Year to 31 Dec	2007	2008	2009F	2010F	2011F
Revenue (RMB mn)	1,845	3,693	5,776	10,815	13,657
Growth (%)	103	100	56	87	26
Net profit (RMB mn)	(267)	131	899	2,492	3,522
Growth (%)	na	na	585	177	41
vs IBES (%)	-	-	(31)	(11)	(8)
EPS (RMB)	(0.57)	0.14	0.13	0.20	0.28
Growth (%)	na	na	(0)	50	41
P/E (x)	na	14.4	14.5	9.6	6.8
P/B (x)	0.8	0.8	2.9	1.8	1.3
EV/EBITDA	77.6	48.9	16.2	7.8	5.9
Yield (%)	0.0	1.0	0.6	1.6	2.9

Source: Bloomberg and Core Pacific - Yamaichi

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Sturdy earnings growth from power business

Stunning 1H09 EPS growth on strong power operation. In contrast with a lower national electricity demand in the 5M09, GCL-Poly still registered an 119 hours yoy increase in average utilization hours to 3,243 hours for the 1H09, with electricity sales volume rising 6.4% yoy to 2,589 GWh, thanks to the green attributes of its power plants, which enjoyed higher power dispatch priority than conventional coal-fired power plants. Steam sales revenue jumped 13% yoy RMB422mn as the 16% yoy increase in steam ASP has more than offset the 2.6% yoy decline in steam sales volume.

Table 1: 1H09 results highlight and comparison

	1H08	2H08	1H09	YoY chg	HoH chg
Revenue	1,787,267	1,906,063	1,951,810	9.2	2.4
Cost of sales	(1,586,729)	(1,609,291)	(1,650,973)	4.0	2.6
Gross profit	200,538	296,772	300,837	50.0	1.4
EBIT	155,569	265,346	243,394	56.5	-8.3
Finance costs	(129,821)	(128,925)	(113,463)	-12.6	-12.0
Results of associate	17,470	27,223	1,865	-89.3	-93.1
Profit before tax	43,218	163,644	131,796	205.0	-19.5
Income tax expense	(5,599)	(21,541)	(16,807)	200.2	-22.0
Profit after tax	37,619	142,103	114,989	205.7	-19.1
Minority interests	(17,114)	(31,310)	(43,142)	152.1	37.8
Net profit	20,505	110,793	71,847	250.4	-35.2

Source: company data and Core Pacific-Yamaichi

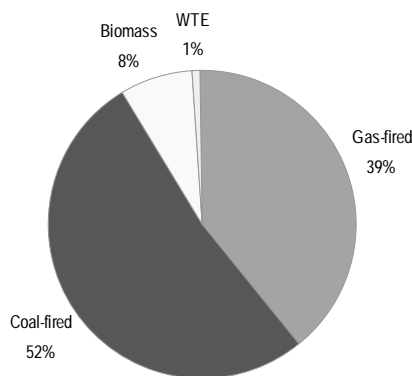
Table 2: 1H09 operation metrics

	1H08	2H08	1H09	YoY chg	HoH chg
Electricity sales volume (GWh)	2,432	2,158	2,589	6.4	19.9
Utilization hour	3,124	2,742	3,243	3.8	18.3
Electricity ASP (RMB/MWh)	540	574	564	4.4	-1.7
Installed capacity (MW)	855	870	876	2.5	0.7
Steam sales volume (ton)	2,727,598	2,636,110	2,656,208	-2.6	0.8
Steam ASP (RMB/ton)	155	192	180	16.1	-6.3
Coal cost (RMB/ton)	467	532	452	-3.2	-15.1

Source: company data and Core Pacific-Yamaichi

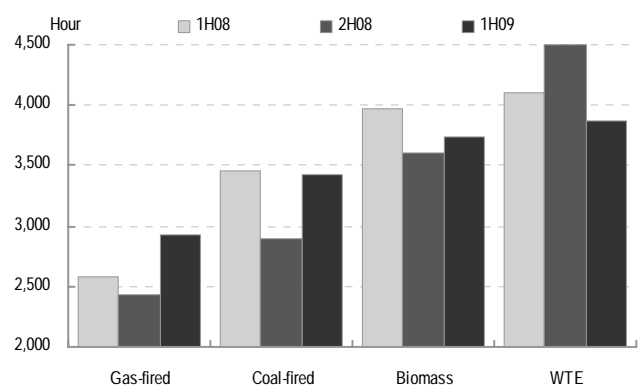
Power business will remain strong momentum in 2H09. We expect GCL-Poly's power business to improve further in 2H09 as power demand growth in the country has returned to positive territory since June 2009 and this should help improve GCL-Poly's utilization rate. Stable spot coal prices and low interest rate should help mitigate the cost pressure in 2H09.

Figure 1: Breakdown of electricity sales by fuel type



Sources: company data

Figure 2: Resilient utilization rate



Sources: company data

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The worst for solar business is over

Slump in polysilicon business in 1H09. In the face of polysilicon price crash in 4Q08, GCL-Poly suffered substantial gross margin contraction in 1H09. 1H09 GPM of polysilicon segment plunged to 41.4%, compared with 72.6% in FY08. The realized polysilicon ASP was US\$80/kg, compared with US\$271/kg for FY08. The sharp plunge in ASP has largely offset the benefits from 1) the decline in average unit production cost, which dropped from US\$66.3/kg for FY08 to US\$43.4/kg for 1H09, and 2) the robust volume sales of 1,917MT for 1H09 (vs FY08: 1,850MT). As such, 1H09 gross profit was only RMB460.5mn, compared with RMB2,555mn for FY08.

Resilient 2H09 driven by explosive volume growth, stable price and lower cost. Management guided the FY09 polysilicon target of 7,500MT could be achieved. GCL-Poly signed long-term contracts with downstream PV module and panel makers to deliver 33,000MT of polysilicon from 2008 to 2020. 2H09 polysilicon sales will be 4,432MT, representing 231% hoh increase. Spot polysilicon prices have stabilized at US\$65-70/kg in recent months and we expect price to stabilize in the rest of the year due to pick up in demand from downstream players. Along with the lower average production cost, we forecasts GPM of polysilicon business to improve to 44.4% in 2H09 from 41.4% in 1H09.

Table 3: Key operational metrics of GCL-Poly's polysilicon business and CPY's revisions

	FY08	1Q09	2Q09	1H09	FY09F (old)	FY09F (new)	Chg (%)
Production capacity (MT)	3,000	5,500	8,000	13,500	18,000	18,000	0.0
Production volume (MT)	1,850	1,094	1,180	2,274	7,800	7,700	-1.3
external sales (MT)	1,530	1,025	892	1,917	7,650	6,349	-17.0
for wafer production (MT)	320	69	288	357	150	1,351	800.9
ASP (US\$/kg)	271	94	63	80	71	69	-1.8
Unit cost (US\$/kg)	(66)	(49)	(39)	(43)	39	39	0.0

Source: company data and Core Pacific-Yamaichi

Chinese government latest policies help control overcapacity. In late August, Chinese premier Wen Jiabao ordered moves be taken to curb overcapacity and the presence of duplicate projects that exist in certain sectors, including the polysilicon industry. The State Council will strictly enforce limits to market access, intensify environmental supervision and strictly controlling land supply for any new projects in these selected industries. We believe the warning about overcapacity in polysilicon industry was targeted at those firms with outdated production facilities, highly environmental-polluting and high-energy consumption. In the latest move, China's Environmental Protection Ministry has imposed ban on importing scrap polysilicon recycled to make solar wafers, with effective from 1 Sep, because the process of recycling the scrap polysilicon causes serious environment pollution problem. In anticipation of more policies to deal with overcapacity, we believe the overcapacity in polysilicon production in China will be eased and this will be conducive to GCL-Poly.

New market potential from electronic grade polysilicon sales has not yet factored in. Management said GCL-Poly plans to trial produce electronic grade polysilicon, which requires higher purity and yield higher profitability, by 2010. Its existing Xuzhou production plant phase III is designed to produce electronic grade polysilicon and is the only plant that is formally recognized by the central government. Management said China imported ~4,000MT electronic grade polysilicon and expect future demand to reach 30,000MT per annum, mainly driven by the strong demand from the central government for developing the aerospace and astronautic industry. However, we have not incorporated this new business into our model unless the details of commercial production can be materialized.

Lower TP to HK\$3.2 on lower profit from polysilicon. Maintain BUY. We have lowered our FY09-11 EPS forecasts by 7%, 5% and 4% respectively as we marginally lower our polysilicon ASP and shipment assumptions. As such, we lower our TP to HK\$3.2 from HK\$3.54, representing FY10F PBR of 2.7x and PER of 14.0x. Concern over overcapacity in polysilicon industry and unproven operating history of GCL Solar keep GCL-Poly's valuations at current depressed levels, in our view. Its shares has corrected by ~42% from its recent high and we believe current price provides a good entry point. Maintain BUY.

Profit & loss (consolidated)

Year to 31 Dec (RMB mn)	2007	2008	2009F	2010F	2011F
Revenue	1,845	3,693	5,776	10,815	13,657
polysilicon		3,000	1,954	5,070	2,825
wafer		521	202	1,996	6,775
power sales	1,470	2,189	2,407	2,524	2,708
steam sales	374	827	862	1,007	1,128
coal trading	0	677	351	218	221
Costs of good sold	(1,482)	(3,196)	(4,160)	(6,790)	(8,367)
Gross profit	362	497	1,617	4,025	5,290
Other income	109	168	127	125	89
Distribution costs	0	(7)	(3)	(2)	(1)
SG&A	(209)	(238)	(406)	(774)	(786)
EBIT	262	421	1,335	3,373	4,593
Finance cost	(162)	(259)	(327)	(447)	(469)
Gains/losses from associate	20	45	4	4	4
Non-recurring items	(337)	0	0	0	0
Profit before tax	(216)	207	1,012	2,931	4,128
Income tax credit (expense)	4	(27)	(46)	(388)	(551)
Minority interests	(55)	(48)	(66)	(51)	(55)
Net profit	(267)	131	899	2,492	3,522
EPS (RMB)	(0.571)	0.135	0.134	0.202	0.285
DPS (HK\$)	0.000	0.023	0.012	0.034	0.065
BVPS (RMB)	2.337	2.484	0.667	1.056	1.516

Cash flow (consolidation)

Year to 31 Dec (RMB mn)	2007	2008	2009F	2010F	2011F
Operating Cash Flow	214	641	2,728	2,819	4,361
Pretax profit	(216)	207	1,012	2,931	4,128
Depre & amort	163	254	703	875	992
Change in wc	(191)	(23)	621	(1,117)	(709)
Others	458	202	392	131	(50)
Investing Cash Flow	(209)	(469)	(8,178)	(3,219)	(2,178)
CAPEX	(255)	(489)	(8,016)	(3,180)	(2,135)
Others	46	20	(162)	(39)	(43)
Free Cash Flow	5	172	(5,451)	(535)	1,809
Financing Cash Flow	624	(550)	6,119	923	(1,334)
Equity financing	1,049	2	3,500	0	0
Chg in bank loans	179	(230)	5,288	1,593	(395)
Dividend	0	0	(20)	(135)	(374)
Others	(604)	(321)	(2,669)	(536)	(565)
Net Cash Flow	628	(378)	668	523	849
Cash at end	804	414	1,074	1,672	2,487

Key assumptions

Year to 31 Dec	2007	2008	2009F	2010F	2011F
Power business					
Installed capacity (MW)	840	870	941	989	1,004
Steam Extraction (ton/hr)	1894	2,199	2,249	2,367	2,412
Power sales (GWh)	3,726	4,591	4,832	4,854	5,210
Steam sales (ton,000)	3,040	5,364	5,367	6,228	6,669
Ave utilization hours	6,173	5,866	5,856	5,530	5,761
Ave power tariff (RMB/MWh)	427	477	512	520	520
Ave steam price (RMB/ton)	120	154	162	165	173
Ave coal cost (RMB/ton)	620	786	714	759	796
Solar business					
Poly ASP (US\$/kg)		271	69	63	59
Wafer ASP (US\$/Wp)		1.90	0.77	0.73	0.71
Poly unit cost (US\$/kg)		66	38	34	33
Poly shipment (MT)		1,530	6,349	11,800	7,020
Wafer shipment (MW)		39	52	400	1,400

Balance sheet (consolidated)

As at 31 Dec (RMB mn)	2007	2008	2009F	2010F	2011F
Total Assets	6,867	7,070	22,824	26,072	28,458
Current Assets	1,748	1,407	2,941	3,825	5,005
Cash at banks	804	414	1,074	1,672	2,487
Accounts receivable	547	468	661	873	1,159
Inventory	126	259	243	268	295
Others	271	266	964	1,013	1,064
Non-current Assets	5,119	5,662	19,882	22,247	23,453
Net fixed assets	4,658	4,948	12,252	14,568	15,722
Prepaid lease payment	234	228	390	430	474
Intangible assets	131	130	6,862	6,862	6,862
Interests in associates	73	245	219	222	223
Others	23	111	159	165	172
Total Liabilities	4,230	4,246	14,151	12,569	9,240
Current Liabilities	2,157	2,542	6,054	6,329	4,643
Bank borrowings	1,492	1,652	3,288	4,461	3,212
Accounts payable	615	827	2,544	1,628	1,172
Due to related companies	46	54	171	189	208
Others	5	8	51	51	51
Long-term Liabilities	2,073	1,704	8,097	6,240	4,597
Bank borrowings	1,988	1,597	5,250	4,461	3,212
Convertible notes	0	0	793	793	793
Others	85	107	2,054	986	592
Total Equity	2,637	2,824	8,672	13,502	19,218
Shareholders' equity	2,273	2,416	8,248	13,052	18,736
Minority interests	364	408	425	450	482
Net cash / (debt)	(2,676)	(2,836)	(7,464)	(7,250)	(3,936)
Net working capital	(410)	(1,135)	(6,054)	(6,329)	(4,643)
Total capital invested	6,201	6,180	20,057	24,203	27,027

Key ratios

Year to 31 Dec	2007	2008	2009F	2010F	2011F
Momentum (%)					
Revenue	103	100	56	88	26
Gross profit	82	37	225	150	31
EBIT	57	60	217	154	36
Net profit	na	na	584	179	41
EPS	na	na	(1)	51	41
Margin (%)					
Gross profit	19.6	13.5	28.0	37.2	38.7
EBIT	14.2	11.4	23.1	31.2	33.6
Net profit	-14.5	3.6	15.5	23.1	25.7
Return (%)					
ROIC	4.2	5.9	6.3	12.1	14.7
ROE	-11.7	5.4	10.9	19.2	18.8
ROA	-3.9	1.9	3.9	9.6	12.4
Financial risk (%)					
Net gearing	118	117	91	56	21
Interest coverage (x)	1.6	1.6	4.1	7.6	9.8
Liquidity (x)					
Current ratio	0.8	0.6	0.5	0.6	1.1
Quick ratio	0.8	0.5	0.4	0.6	1.0
Others (%)					
Effective tax rate	2	13	5	13	13
Payout ratio	0	15	15	15	20

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