



China Sunshin Chemical Hld Ltd

(CSSC SP/CHSN.SI)

Robust amidst cyclical downturn

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- 1H20 profitability weakened substantially due to the unfavourable environment such as declining ASP and profit margin in the sector.
- Near-term demand could be compressed as tyre manufacturers have yet to recover to pre-COVID levels.
- Zero-debt and abundant cash in hand, together with positive free cash flow, enable Sunshin to endure the down cycle.
- We maintain **OUTPERFORM** with a lower TP of \$0.47 due to the near-term headwinds of declining ASP and profit margin compression. It is worth noting that the cash per share as of June 2020 was S\$0.27.

Financials & Key Operating Statistics

YE Dec (RMB m)	FY17	FY18	FY19	FY20F	FY21F
Revenue	1695.9	3283.3	2691.6	2205.9	2540.1
PATMI	341.3	641.3	388.9	187.0	249.2
Core PATMI	341.3	593.3	388.9	187.0	249.2
Core EPS (RMB cents)	70.8	120.7	79.7	19.2	25.6
Core EPS grth (%)	48.6	70.4	-34.0	-75.9	33.2
Core P/E (x)	4.8	2.8	4.3	8.9	6.7
DPS (SGCents)	3.0	5.5	1.0	0.8	1.0
Div Yield (%)	9.0	16.4	3.0	2.3	3.1
Net Margin (%)	12.5	19.5	14.4	8.5	9.8
Gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Price / Earnings (x)	4.8	2.8	4.3	8.9	6.7
Price / Book (x)	1.0	0.7	0.7	0.6	0.6
ROE (%)	19.6	27.6	15.3	7.0	8.6

Source: Company Data, KGI Research

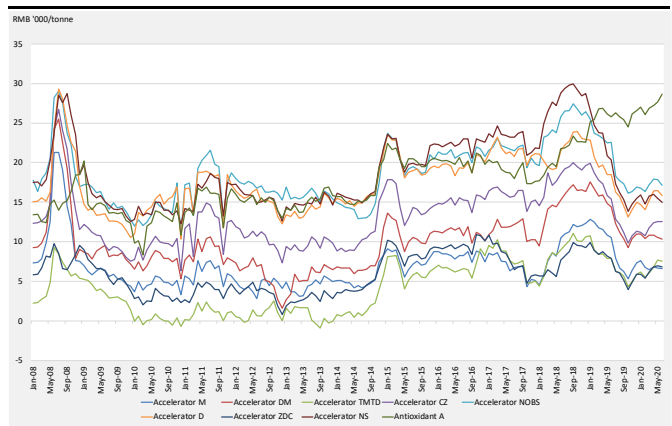
Enduring through adversities in the down cycle. Rubber chemicals prices completed a bull-bear cycle after the global financial crisis in 2008. To illustrate the cyclical expansion and decline of profit margin in the sector, we used the average selling price (ASP) spread between rubber chemicals and the main raw materials aniline as a proxy. The peak-to-peak period lasted exactly a decade, reflecting that the sector went through over-capacity and the ensuing supply-side reform in China. Driven by the high profit margins, main producers ramped up capacity in 2017 and early 2018, and the incremental supply was put in the market, marking the beginning of the down cycle in 4Q18. Unfortunately, the COVID-19 pandemic further disrupted the supply and demand balance.

China Sunshin changed to semi-annual reporting this year. 1H20 profitability weakened substantially compared to 1H19, due mainly to the unfavourable macro environment resulting in contraction in both ASP and profit margins. However, normalisation of profit margin and correction of ASP were expected by the management back in 2018 and 2019.

Outperform - Maintain

Price as of 18 Aug 20 (SGD)	0.34	Performance (Absolute)	
12M TP (\$S)	0.47	1 Month (%)	-4.3
Previous TP (\$S)	0.60	3 Month (%)	-7.1
Upside (%)	40.3	12 Month (%)	-35.2
Trading data		Perf. vs STI Index (Red)	
Mkt Cap (\$mn)	326		
Issued Shares (mn)	972		
Vol - 3M Daily avg (mn)	0.7		
Val - 3M Daily avg (\$mn)	0.3		
Free Float (%)	37.9%		
Major Shareholders		Previous Recommendations	
Success More Group	60.1%	11-Oct-19	OP \$0.7
Dimensional Fund Advisor	1.3%	18-Nov-19	OP \$0.6
Phoenician Capital LLC	1.0%		

Figure 1: ASP spread between rubber chemicals and aniline



Source: Company, KGI Research

Valuation & Action: We maintain our **OUTPERFORM** recommendation with a lower target price of \$0.47 due to the near-term headwinds of declining ASP and profit margin compression. It is worth noting that the cash per share as of June 2020 was S\$0.27.

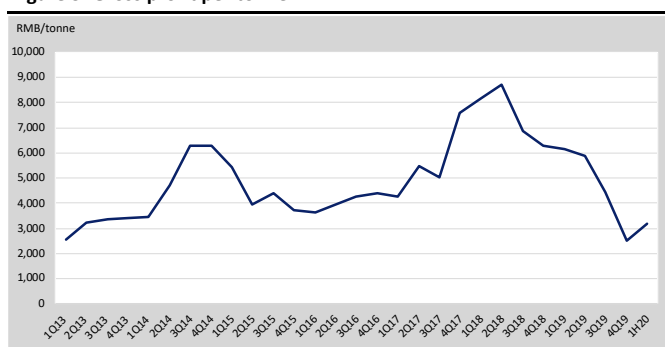
Risks: The risk is the prolonged downturn of the cycle. China Sunshin as the market leader in rubber chemicals industry in China, has been occupying the majority of the market share in both domestic and overseas markets. However, investors should know that the company lacks catalysts apart from the ramp-up of production which depends on market conditions. The difference from the 2017-2018 period when it was tagged as a growth stock, enjoying both substantial volume and ASP growth, is that Sunshin is now regarded as a value stock. Therefore, the likely driver of higher price performance lies on the turnaround of macro conditions such as the bottoming-out of ASP and the exit of more peers from the market. The recovery of the economy should lead to improvement in profitability but not to what it was during the heydays.

Figure 2: 1H20 results comparison

Financials (RMB mn)	1H20	1H19	YoY change
Revenue	1,043	1,414	-26%
Gross profit	242	488	-50%
PAT	82	266	-69%
Profit margin	1H20	1H19	Percentage points change
GPM	23.2%	34.5%	-11.3
NPM	7.9%	18.8%	-10.9
Sales volume (tonne)	1H20	1H19	YoY change
Accelerators	40,480	43,790	-8%
Insoluble Sulphur	13,333	14,930	-11%
Anti-oxidant	21,564	22,385	-4%
ASP (RMB/tonne)	1H20	1H19	YoY change
Accelerators	16,173	21,770	-26%
Insoluble Sulphur	7,553	9,424	-20%
Anti-oxidant	12,359	13,089	-6%

Source: Company, KGI Research

Figure 3: Gross profit per tonne



Source: Company, KGI Research

Moderately positive outlook in 2H20. In 2H20, China will likely remain cautious of sporadic imported spread of COVID-19, and will look to a gradual reopening of borders. Productions and business is expected to continue to recover, but the external demand may not catch up soon as the pandemic is not yet contained. Therefore, growth must rely on domestic demand. However, tyre manufacturers' utilisation rate has not recovered to pre-COVID levels. The weak demand could be prolonged in the near term.

Figure 4: China rubber chemicals sector periodic performance comparison

	1H20	1H19	YoY change
Total production value (RMB bn)	8.4	11.5	-27%
Total sales (RMB bn)	8.8	11.0	-20%
Export value (RMB mn)	188	350	-46%
Total production volume ('000 tonnes)	575	667	-14%
Accelerators	150	202	-26%
Anti-oxidant	154	189	-19%
Export volume ('000 tonnes)	120	185	-35%

Source: China Rubber Industry Association, KGI Research

We are cautiously positive on the 2H20 outlook. Firstly, crude oil prices bottomed out in April. Ongoing output cuts and the slow pick-up of oil demand could support oil prices, which will subsequently provide a price floor for chemical products. Secondly, raw material prices like aniline reached a decade low of RMB4,500/tonne recently, and further decline in prices will drive out more small and medium players in the market. In other words, long-lasting ASP below breakeven costs will accelerate the balance of supply and demand dynamics. Lastly, China SunSine is robust enough to endure the down cycle. It

has a clean balance sheet with zero debt and abundant cash (RMB1.3bn as of June 2020, equivalent to S\$0.27/share). Its cash flows from operations are firmly positive and enough to cover capex.

Production forecast and valuation

Figure 5: Main product sales volume and ASP forecast

	FY19	FY20F	FY21F
Sales volume (tonnes)			
Accelerators	88,261	85,600	99,450
Insoluble Sulphur	29,916	27,900	28,500
Anti-oxidant	47,284	42,750	42,750
Realised ASP (RMB/tonne)			
Accelerators	19,847	16,473	17,297
Insoluble Sulphur	8,945	7,782	8,016
Anti-oxidant	13,161	12,503	12,753
Sales (RMB mn)			
Accelerators	1,752	1,410	1,720
Insoluble Sulphur	268	217	228
Anti-oxidant	622	534	545

Source: KGI Research

Figure 6: DCF model

RMB mn	FY20F	FY21F	FY22F
Net income	187	249	279
Net capex	(150)	(120)	(100)
Change in net WC	42	39	41
Change in borrowing	-	-	-
FCFE	79	168	220
Beta	1.02		
Required rate of return	9.2%		
Growth	0.5%		
FX (SGD/RMB)	5.10		
TP (SGD)	0.47		

Source: KGI Research

YE 31 Dec

INCOME STATEMENT (RMB m)	FY17	FY18	FY19	FY20F	FY21F
Revenue	2,738	3,283	2,692	2,206	2,540
Cost of sales	(1,950)	(2,157)	(1,911)	(1,699)	(1,905)
Gross Profit	788	1,126	781	507	635
EBITDA	567	809	567	381	472
Depreciation & Amortisation	90	98	114	121	126
EBIT	477	712	453	260	346
Profit from Operations	477	712	453	260	346
Net Finance (Expense)/Inc	-	-	(1)	(0)	-
Profit before Tax	477	712	453	260	346
Income tax	(136)	(70)	(64)	(73)	(97)
PAT	341	641	389	187	249
PAT Normalized	341	593	389	187	249

BALANCE SHEET (RMB m)	FY17	FY18	FY19	FY20F	FY21F
Cash and bank balances	500	1,039	1,279	1,425	1,681
Inventories	212	217	247	199	182
Trade receivables	638	691	525	502	514
Others	75	70	139	160	171
Current Assets	1,425	2,016	2,190	2,285	2,548
PP&E	662	691	650	680	675
Others	41	40	39	38	37
Non-current Assets	703	731	689	718	711
Total assets	2,128	2,747	2,878	3,003	3,259
Trade payables	71	63	64	54	64
Borrowings	-	-	-	-	-
Others	314	359	283	269	293
Current Liabilities	385	422	347	323	357
Bank loans	-	-	-	-	-
Non-current liabilities	-	-	-	-	-
Shareholders equity	1,742	2,326	2,542	2,689	2,910
Total Equity	1,742	2,326	2,542	2,689	2,910
Total Liabilities and Equity	2,128	2,747	2,888	3,012	3,267

CASH FLOW STATEMENT (RMB m)	FY17	FY18	FY19	FY20F	FY21F
Profit before tax	477	712	453	260	346
Depreciation & non cash adjustments	90	98	114	121	126
Change in Working Capital	(83)	(2)	20	42	39
Income Tax Paid	(100)	(84)	(121)	(73)	(97)
Interest Paid	-	-	0	0	-
Others	2	(22)	(18)	(18)	(18)
CF from operating activities	387	701	448	332	396
Purchase/Disposal of PPE	(209)	(130)	(72)	(150)	(120)
Others	4	4	13	18	18
CF from investing activities	(205)	(125)	(59)	(132)	(102)
Dividends Paid	(47)	(59)	(136)	(49)	(38)
Debt Raised / (Repaid)	-	-	-	-	-
Equity Raised / (Bought Back)	86	(2)	(20)	(5)	-
Others	10	8	1	-	-
CF from financing activities	50	(52)	(154)	(54)	(38)
Net increase in cash & cash equiv.	231	523	235	146	256
FX effects	(9)	16	9	-	-
Beginning Cash	274	496	1,035	1,279	1,425
Ending Cash	496	1,035	1,279	1,425	1,681

KEY RATIOS	FY17	FY18	FY19	FY20F	FY21F
Profitability					
Core EPS	70.8	120.7	79.7	19.2	25.6
Core EPS Growth (%)	48.6	70.4	(34.0)	(75.9)	33.2
DPS (SGD Cents)	3.0	5.5	1.0	0.8	1.0
Dividend Yield (%)	9.0	16.4	3.0	2.3	3.1
Profitability					
Gross margin	28.8%	34.3%	29.0%	23.0%	25.0%
EBITDA margin	20.7%	24.6%	21.1%	17.3%	18.6%
Net margin	12.5%	19.5%	14.4%	8.5%	9.8%
ROE	19.6%	27.6%	15.3%	7.0%	8.6%
ROA	16.0%	23.3%	13.5%	6.2%	7.6%
Financial Structure (x)					
Interest coverage	-	-	-	-	-
Total Debt/Equity	-	-	-	-	-
Net Gearing	Net cash	Net cash	Net cash	Net cash	Net cash
Market Valuation (x)					
Price / Earnings	4.8	2.8	4.3	8.9	6.7
Price / Book	1.0	0.7	0.7	0.6	0.6
EV / EBITDA	2.2	1.6	2.2	3.3	2.6

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