

CHINA CERAMICS CO., LTD.

4Q & FYE 2016 Earnings Call

May 15, 2017

8:00 a.m. ET

Speakers:

Mr. Jaidong Huang, CEO

Mr. Edmund Hen, CFO

Operator: Good afternoon. My name is Armika and I'll be your conference operator today. At this time, I would like to welcome everyone to the China Ceramics fourth quarter and fiscal year end 2016 earnings conference call.

All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question and answer session. If you like to ask a question during this time, simply press star then the number one on your telephone keypad. If you will like to withdraw your question, press the pound key.

Thank you. I'll now turn the conference over to Mr. David Rudnick of Precept Investor Relations. Please go ahead, sir.

David Rudnick: Good morning ladies and gentlemen and good evening to those of you who are joining us from China. Welcome to China Ceramics' Welcome to China Ceramics' fourth quarter and fiscal year end 2016 earnings conference call. With us today are China Ceramics Chairman and Chief Executive Officer, Mr. Jiadong Huang and its Chief Financial Officer, Mr. Edmund Hen.

Before I turn the call over to Mr. Huang, I would like to address forward-looking statements that may be discussed on the call. Forward-looking statements involve risks and uncertainties and include, among others, those regarding revenue, operating expenses, other income and expense, taxes, and future business outlook. Actual future performance, outcomes and results may differ materially from those expressed in forward-looking statements. The Company claims the safe harbor protections for such forward-looking statements as contemplated under the Private Securities Litigation Reform Act of 1995. Please refer to the documents filed by the Company with the SEC,

specifically the most recent reports on Forms 20-F and 6-K, which identify important risk factors that could cause actual results to differ from those contained in the forward-looking statements. We assume no obligation to update any forward-looking statements or information, which speak as of their respective dates.

On today's call, we will reference certain non-GAAP financial measures. In accordance with SEC rules, we have provided a reconciliation of these non-GAAP measures to their most directly comparable GAAP measures in our earnings release and financial supplements, which can be found on the Investor Relations portion of the Company's corporate website. To supplement the financial results presented in accordance with U.S. GAAP, management will make reference to, among others, Earnings before Interest, Taxes, Depreciation and Amortization, which we will call by its abbreviated name, "EBITDA". EBITDA is a non-GAAP financial measure reconciled from net income, which the company believes provides meaningful, additional information to better understand its operating performance. A table reconciling net income to EBITDA can be found in the earnings press release issued earlier today.

And now it's my pleasure to turn the call over to China Ceramics' Chairman and CEO, Mr. Jiadong Huang and China Ceramics' CFO, Mr. Edmund Hen. Weijia Dai will be translating for Mr. Huang. Mr. Huang, you may proceed.

Jiadong Huang: (In Chinese)

Weijia Dai: Thank you, David. On behalf of the company, I would like to welcome everyone to our fourth quarter and fiscal year end 2016 earnings conference call.

Jiadong Huang: (In Chinese)

Weijia Dai: We continued to experience challenging market conditions in both the fourth quarter and fiscal 2016 due to macroeconomic factors that have continued to

negatively impact the China real estate and building materials markets. However, excluding the impact of the impairment charges, inventory write downs, and increases in the provision for bad debt taken during the period, we were able to generate \$8.4 million in EBITDA for fiscal 2016. In addition, in order to generate sales and move inventory, beginning on October 1st, 2016, we instituted a 20% reduction in the prices of slow moving products which helped to turn some of our inventory into cash. This price reduction led to a 35% increase in our sales volume in the fourth quarter compared to the same period in 2015. We are also looking for ways to operate more efficiently by running production lines concurrently with the generation of customer orders.

Jiadong Huang: (In Chinese)

Weijia Dai: We continued to experience challenging market conditions in both the fourth quarter and fiscal 2016 due to macroeconomic factors that have continued to negatively impact the China real estate and building materials markets. However, excluding the impact of the impairment charges, inventory write downs, and increases in the provision for bad debt taken during the period, we were able to generate \$8.4 million in EBITDA for fiscal 2016. In addition, in order to generate sales and move inventory, beginning on October 1st, 2016, we instituted a 20% reduction in the prices of slow moving products which helped to turn some of our inventory into cash. This price reduction led to a 35% increase in our sales volume in the fourth quarter compared to the same period in 2015. We are also looking for ways to operate more efficiently by running production lines concurrently with the generation of customer orders.

Jiadong Huang: (In Chinese)

Weijia Dai: During the fourth quarter, we utilized production facilities capable of producing 37 million square meters of ceramic tiles per year out of the Company's effective annual production capacity of 62 million square meters. As we have in past quarters, we maintained a reduced utilization of existing plant capacity based on the current market conditions to keep our operating costs low, and we will bring additional capacity online when we see an increase in demand for our products.

Jiadong Huang: (In Chinese)

Weijia Dai: Looking ahead to 2017, we believe that the operating environment will slowly begin to improve. Should this occur, we believe that we can leverage our market positioning to maintain our existing customers and win new customers. We expect the consolidation trend among larger property developers to continue which will benefit the Company since our manufacturing scale and infrastructure enable us to effectively service these large enterprises. In the long-term, we believe that real estate is a key sector of China's economy and that the real estate market's supply and demand dynamics will stabilize to present us with sustainable growth opportunities.

With that, I would like to turn over the call to the Company's Chief Financial Officer, Mr. Edmund Hen, who will discuss the Company's fourth quarter earnings results in more detail. Thank you!

Edmund Hen: Thank you Mr. Huang! I will now move on to a more detailed discussion of our financial results for the fourth quarter and fiscal year 2016.

Our revenue for the fourth quarter ended December 31, 2016 was RMB 201.9 million, or US\$ 28.3 million, a decrease of 3.1% from RMB 208.3 million, or US\$ 31.6 million in the fourth quarter of 2015. The year-over-year increase in revenue was primarily due to a 28.2% decrease in our average selling price in the fourth quarter of 2016 to RMB 22.4 or US\$ 3.2 as compared to RMB 31.2 or US\$ 4.1 for the fourth quarter of 2015, partially offset by a 34.8% increase in sales volume to 9.0 million square meters of ceramic tiles in the fourth quarter of 2016 from 6.7 million square meters in the fourth quarter in 2015.

Gross loss for the fourth quarter ended December 31, 2016 was RMB 87.1 million or US\$ 13.2 million as compared to profit of RMB 29.5 million or US\$ 4.5 million for the fourth quarter of 2015. The gross profit margin was a negative 43.1% for the fourth quarter ended December 31, 2016 compared to 14.2% for the fourth quarter of 2015. The year-over-year reduction in gross profit margin was primarily due to a 28.2% decrease in the average selling price of the Company's ceramic tiles attributable to our having instituted a

20% reduction in the selling prices of slow moving inventory beginning on October 1st, 2016, due to challenging market conditions, and an RMB 59.4 million or US\$ 8.9 million write down of inventory in the fourth quarter of 2016.

Other income for the fourth quarter ended December 31, 2016 was RMB 3.5 million or US\$ 0.5 million, as compared to RMB 0.1 million or US\$ 0.01 million for the fourth quarter of 2015. The year-over-year increase in other income was mainly caused by rental income of RMB 3.5 million or US\$ 0.5 million the Company received by leasing out one of its production lines from its Hengdali facility pursuant to an eight-year lease contract.

Selling and distribution expenses for the fourth quarter ended December 31, 2016 were RMB 3.0 million or US\$ 0.4 million as compared to RMB 6.0 million or US\$ 0.9 million in the fourth quarter of 2015. The year-over-year decrease in selling and distribution expenses was primarily due to an RMB 2.7 million or US\$ 0.4 million decrease in advertising expenses and an RMB 0.3 million or US\$ 0.04 million decrease in travelling and entertainment expenses.

Administrative expenses for the fourth quarter ended December 31, 2016 were RMB 29.4 million or US\$ 4.3 million as compared to RMB 6.2 million or US\$ 1.0 million in the fourth quarter of 2015. The year-over-year increase in administrative expenses was primarily due to an RMB 24.0 million or US\$ 3.5 million provision for bad debt.

The loss from operations before taxes for the fourth quarter of 2016 was RMB 351.6 million or US\$ 52.5 million as compared to a RMB 406.5 million or US\$ 64.2 million of loss from operations before taxation in the fourth quarter of 2015. The year-over-year decrease in profit from operations before taxation was attributable to an impairment of non-current assets of RMB 230.4 million or US\$ 34.3 million, an inventory write-down of RMB 59.4 million or US\$ 8.9 million, and a provision for bad debt of RMB 24.0 million or US\$ 3.5 million. In the fourth quarter of 2015, there was an impairment of non-current assets of RMB 421.6 million or US\$ 66.5 million which caused a loss from operations before taxes for that quarter.

Net loss for the fourth quarter of 2016 was RMB 352.5 million or US\$ 52.6 million as compared to RMB 411.3 million or US\$ 64.9 million of net loss for the fourth quarter ended December 31, 2015.

Loss per fully diluted share for the fourth quarter of 2016 on a basic and fully diluted basis were RMB127.63 or US\$ 19.05 as compared to basic and fully diluted earnings per share of RMB 161.04 or US\$ 24.88 in the fourth quarter of 2015, as adjusted for the one for eight reverse split in June 2016.

For the full-year ended December 31, 2016, revenue was RMB 793.7 million or \$118.3 million, a decrease of 22.0% as compared to RMB 1,017.1 million or \$160.4 million for the full year 2015. Gross loss was RMB 30.1 million or \$4.5 million, as compared to gross profit of RMB 125.4 million or \$19.8 million. Gross margin for the full-year 2016 was a negative 3.8% compared to 12.3% for the full-year 2015. Net loss for fiscal 2016 was RMB 321.8 million or US\$ 48.0 million as compared to a net loss of RMB 362.4 million or US\$ 57.2 million for fiscal year 2015. The loss per basic share and earnings per fully diluted share were RMB 116.51 or US\$ 17.36 for the year ended December 31, 2016, as compared to loss per basic and fully diluted share of RMB 141.91 or US\$ 21.92 for the same period of 2015, as adjusted for the one for eight reverse stock split in June 2016.

Turning to our balance sheet, as of December 31, 2016, we had cash and bank balances of RMB 0.1 million, or US\$ 0.01 million, as compared to RMB 0.5 million or US\$ 0.1 million as of fiscal year end 2015. Our short-term bank borrowings were nil, as compared to RMB 40.1 million or US 6.2 million as of fiscal year end 2015.

As of December 31, 2016, our inventory turn was 115 days compared to 131 days as of December 31, 2015. Our trade receivables turnover was 245 days compared with 163 days as of fiscal year end 2015. The increase in trade receivables turnover days was primarily due to the difficult economic environment which has prompted us to offer extended credit terms to certain customers resulting in a higher trade receivables turnover figure than normal.

In the fourth quarter of 2016, the Company accrued RMB 23.9 million or US\$ 3.5 million as a provision for bad debt for bad debt related to the outstanding trade receivables that did not conform with the Company's credit policy. Trade payables turnover, net of value added tax, was 43 days as of December 31, 2016 compared with 70 days as of December 31, 2015. The average turnover days was within the normal credit period of one to four months granted by our suppliers.

In terms of our plant utilization and capex, for the fourth quarter of 2016, we utilized plant capacity capable of producing 37 million square meters of ceramic tiles annually out of a total annual production capacity of 62 million square meters of ceramic tiles. Our annual production capacity has been effectively reduced from 72 million square meters of ceramic tiles to 62 million square meters of ceramic tiles due to an eight-year contract to lease out one of our production lines from our Hengdali facility that we entered into in March 2016. The current quarter's utilization represents an increase in plant capacity utilization from the fourth quarter of 2015, when we utilized plant capacity capable of producing 26 million square meters of ceramic tiles annually. Although business conditions are subject to change, looking ahead to 2017, we anticipate a low level of capital expenditures given the currently challenging market conditions.

Moving on to our business outlook, to help mitigate the effects of the continued slowdown in China's construction sector and its effect on the Company's building materials sector, on October 1st, 2016, we instituted a 20% reduction in the prices of slow moving inventory. This resulted in a 34.8% increase in our sales volume to 9.0 million square meters of ceramic tiles compared to sales volume of 6.7 million square meters of ceramic tiles in the fourth quarter of 2015. The current quarter's growth in sales volume was the first positive comparison to the previous comparable period after four straight quarters of period over year-ago period declines in this key metric. However, reflective of the industry-wide retrenchment, for the full year 2016, sales volume was 28.8 million square meters of ceramic tiles, a decrease of 12.9% as compared to sales volume of 33.1 million square meters for the same period of 2015.

The 20% reduction in the prices of slow moving inventory that we instituted was primarily the cause of a 28.2% decrease in the average selling price or ASP for all our products in the current quarter to RMB 22.4 or US\$ 3.2 per square meter of ceramic tile as compared to RMB 31.2 or US\$ 4.1 per square meter of ceramic tile in the year-ago quarter. This follows a 10.7% decline in ASP in the third quarter of 2016 preceded by eleven straight quarters of moderate period over year-ago period increases in this metric. The decrease in ASP in the fourth quarter was also the biggest such decline in three years, which was then also due to an industry-wide retrenchment. We chose to discount our slow-moving inventory as means to address the difficult macroeconomic and real estate conditions in China.

Looking ahead to 2017, we expect challenging conditions in the short-term, but improving market conditions as the year progresses. We believe that the real estate and the construction and building materials sectors continue to be vital to sustaining China's economic growth as it is estimated to comprise between 15% and 20% of China's gross domestic product. The demand for home properties continues to be strong in many Tier 1 and 2 cities, both for residential use and investment purposes. Although there remains a substantial level of unsold properties of inventories in smaller cities, housing sales have increased in Tier 3 and 4 cities with the occasional support of subsidies, though this sales increase has been significantly smaller than in larger cities. Further, additional land is being made available for development to rebalance supply and demand and to dampen increases in property prices in China's major cities.

We typically receive orders from customers two months in advance of production on a rolling basis. We enter into dealership agreements with customers, and a sales or purchase contract each time a customer places an order. As of December 31, 2016, our backlog was approximately RMB 61.4 million or US\$ 8.9 million, which represents approximately the next two months of revenue as of the end of the fourth quarter. This compares to a backlog of approximately RMB 66.8 million or US\$ 10.3 million as of December 31, 2015, a year-over-year decrease of 8.0%. Generally, , our

backlog is an indicator of revenues that might be expected in the next quarter, though it is subject to change due to unforeseen business conditions and events including credit payment terms.

In order to weather the current market downturn, we are operating as leanly as possible, keeping our inventory levels manageable with our production of ceramic tiles occurring at the level where we expect to sell them. Our specific niche of the building materials sector is currently characterized as having excessive production capacity where consolidation is occurring and where we believe larger market participants such as China Ceramics will ultimately succeed. Competitive pressures over the last two years has led to a contraction in our sector as some smaller, less well capitalized firms who lack our advanced manufacturing capabilities and deep product platform have exited the space. Additional exits appear likely as government mandates to convert to cleaner and more expensive fuel sources to lower carbon emissions that will also pressure smaller competitors.

In the long-term, we view the growth of the real estate sector and our building materials sector as sustainable since it is underpinned by urbanization which is expected to lead to a more consumption-driven economy, a key objective of government policy. We believe that our branding and market presence will enable us to generate improved financial results once the building materials sector recovers. We have refocused our efforts towards cities in China where we see active real estate development and where property developers use our products as part of their finished home products. We believe we have a competitive advantage in our sector due to our comprehensive product platform, customization capabilities, marketing expertise and ability to implement operating efficiencies. Our goal for the year ahead is to continue to strategically market in regions with sound fundamentals and generate sustainable sales volume until the current period of market volatility subsides.

At this point, we would like to open up the call to any questions pertaining to the fourth quarter and fiscal year 2016 financial and operating performance. Operator?

Operator: Ladies and gentlemen as a reminder, to ask an audio question, please press star one on your telephone keypad.

Operator: The first question comes from Howard Flinker with Flinker & Co.

Howard Flinker: [In Chinese]

Could you please tell me what the effect will be on you and your local competitors of the increase in the environmental tax coming in January, I believe?

Edmund Hen: What we have seen is the more and more small players to have difficulties after this Chinese New Year.

Howard Flinker: And the tax will go up January 1, and another time will it not?

Edmund Hen: We haven't. This is not officially important to us yet.

Howard Flinker: Well other industries have told me that, that's going to happen. So maybe you haven't been told yet, if it does, could it affect some of your bigger competitors too?

Edmund Hen: If the new condition is passed to the other industry, I think everybody will have some impact of that.

Howard Flinker: Even big guys, not just little guys?

Edmund Hen: Even big guys, but it would have most of the negative impact is for the small guys.

Howard Flinker: Sure. And you said, there are some early signs that '17 could be better than '16. What makes you feel that?

Edmund Hen: What we found probably now is the lowest point for the economy in China. So probably from 2016 or next or in 2018 the environment will be better.

Howard Flinker: Okay, those are my only questions. I'll call if I have any other questions. [In Chinese]

Edmund Hen: Thank you.

Operator: Again star one to ask questions. At this time, there are no further questions. Excuse me, we have another question from James Kahn, a private investor.

James Kahn: [In Chinese]. My question is, do you foresee the need to raise capital in 2017, is it through debt or equity. And also, can you – I realize you are talking about the fourth quarter 2016, can you tell us anything yet about the first quarter of 2017 which ended on March 31st, and when will those earnings be released?

Edmund Hen: We are working on the – as you know, we just released this fourth quarter of 2016 and we will immediately work on the first quarter after that. As I see the last year's announcement data was somewhere in June, so we – if we can we will release the first quarter as soon as possible.

James Kahn: Thank you.

Operator: Again, star one to ask questions. At this time, there are no further questions. You may proceed with your closing remarks.

Edmund Hen: Thank you.

Operator: Ladies and gentlemen, this concludes today's conference call. You may now disconnect.

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