**Polysilicon supply ramp up solves key constraint on solar installations**

- New polysilicon supply ramping up in 2H22-2023, removing key overhang on solar value chain
- Solid demand for solar components despite high prices with China’s 2M22 new installations up 234%
- Omicron disruption to production minimal; Government issued directive to unplug transport network
- Normalized solar value chain pricing to benefit solar installations and sales volume of solar components. Top picks: **LONGi** and **Flat Glass**

Resolution of polysilicon bottleneck in sight.
High polysilicon prices have been cited by various solar chain participants as the most important constraint to new installations. A decrease in polysilicon prices should help return the entire solar value chain to more rational pricing. This should remove a key overhang on new solar installations.

New polysilicon capacity ramping up in 2H22-2023.
Major polysilicon producers in China could add 534,000 tonnes of capacity in 2022, up >69% from 2021. With a visible near-term capacity ramp-up, we reckon polysilicon supply tightness should ease in earnest starting 3Q22 and into 2023. Polysilicon production volume could rise c.40% to c.300GW equivalent, more than sufficient to meet our c.246GW forecast of new solar installations globally in 2022. Our channel checks indicate COVID-19 Omicron infections in China had minimal impact on polysilicon production. While logistics had been clogged by pandemic controls, China’s top-level government agencies are actively troubleshooting these blockages.

Rational solar value chain pricing removes overhang on installations. With new polysilicon supply coming to the market, we expect polysilicon prices could soften by c.15% below US$30/kg starting 3Q22. Resolution of the polysilicon bottleneck should benefit overall solar installations, helping demand and sales of solar component manufacturers. Our top picks are LONGi (601012.CH) and Flat Glass (6865.HK, 601865.CH).

**Recommendation & valuation**

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<th>Company Name</th>
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<th>Recom</th>
<th>Mkt Cap US$m</th>
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Source: Thomson Reuters, DBS Bank (Hong Kong) Limited ("DBS HK")
Industry Focus

China Renewable Sector (Solar)

Resolution of polysilicon bottleneck in sight

Polysilicon is one of the most important precursors in the solar value chain, accounting for 87% of COGS for wafers. This translates to roughly 31%-35% of COGS for modules. In 2021, tightened demand-supply led to surging polysilicon prices, which were passed along the solar value chain. High polysilicon prices have been cited by various solar chain participants as the most important constraint to new installations. Our studies indicate a resolution of the supply bottleneck could arrive as early as 3Q22. A decrease in polysilicon prices should help the entire solar value chain return to more rational pricing. This should remove a key overhang on new solar installations.

Supply-demand tightness drove polysilicon price spike.

Polysilicon prices have spiked as high as US$37.4/kg in Dec 21, up c.497% from the low price of US$6.27/kg reached during the depths of the COVID-19 crisis in May-20. The latest price of c.US$34.2/kg is c.9% from the peak. The price spike was due to a tightening of the demand-supply relationship. Polysilicon production growth lagged new solar installations in 2021, as new polysilicon plants can take up to 18-24 months to come online. On the demand side, global new solar installations had grown 28% y-o-y to an estimated c.185GW in 2021, or 214GW. This assumes 2.73 grams of polysilicon per watt. Supply tightness was further exacerbated by China’s power curbs in 3Q21 which temporarily disrupted the supply of silicon metal. The power curbs were resolved with the Chinese government introducing measures to improve coal fuel supply to thermal power generation companies. Polysilicon is formed by purifying silicon metal. Looking ahead, BNEF estimates polysilicon production to rise c.39% y-o-y to c.818,000 tonnes in 2022 or c.300GW equivalent. This should be sufficient and/or exceed our forecast of c.246GW of new solar installations globally in 2022.

New polysilicon capacity ramping up in 2H22-2023.

According to BNEF, global commissioned polysilicon production capacity rose 14% y-o-y to c.768,800 tonnes/year in 2021. Starting in 2H22, major polysilicon producers will begin to ramp up their new capacity. We compiled announcements by major China-based polysilicon players GCL Poly, Tongwei, Daqo, and Xinte. These four players together account for >56% of 2021 global polysilicon production capacity according to BNEF. By end of 2022, these players could add 534,000 tonnes to nameplate capacity. If fully commissioned, this represents an increase of at least 69% y-o-y from 2021.

GCL Poly (3800.HK) is planning to add up to 230,000 tonnes/year in granular silicon capacity starting in 2H22. This consists of 100,000 tonnes in Sichuan (commencing production in 3Q22), 30,000 tonnes in Jiangsu (3Q22), and 100,000 tonnes in Inner Mongolia (4Q22). Tongwei (600438.CH) is planning to add 170,000 tonnes in 2022. This consists of 50,000 tonnes in Inner Mongolia and 120,000 tons in Sichuan. Xinte Energy (1799.HK) has announced plans to add 134,000 tonnes to its capacity in 2022. Xinte expects to complete the renovation of its existing facilities in 1H22, which could add c.34,000 tonnes of capacity. In Inner Mongolia, Xinte is also constructing a 100,000-tonne polysilicon project which is targeted to become operational in 2H22.

Looking further ahead, Xinte plans to add up to 200,000 tonnes at its Xinjiang project in phases between 2023-24.
Industry Focus

China Renewable Sector (Solar)

Daqo New Energy (DQ.US) commenced construction of a 100,000-tonne polysilicon project in Inner Mongolia, with completion targeted in 3Q23. With visible near-term capacity ramp-ups, we reckon the polysilicon supply tightness should ease in earnest starting in 3Q22 and into 2023. This should lead polysilicon prices to soften c.15% to <US$30/kg. All else equal, COGS savings from 15% lower polysilicon prices could drive 9ppts/4ppts gross margin expansion for wafer/modules.

Demand for solar in Europe should remain firm in view of the Ukraine-Russia conflict. The European Union is actively looking to reduce dependency on Russian fossil fuels. On 20 April, the European Commission said it was studying plans for the EU to achieve 45% share of renewable energy by 2030, up from the previously proposed 40%. Our most recent forecast for EMEA solar installations is c.43GW in 2022. Given the increased urgency to diversify its energy mix, we reckon there could be 5-10% upside to this figure.

Solid demand for solar components. Solar component manufacturers have observed strong demand for their products from within China and overseas. Module maker Jinko Solar (JKS.US) has expressed confidence in global solar installations, highlighting strong demand from Europe and India. JKS sees 2022 global new solar installations reaching c.250GW, exceeding our current forecast of c.246GW. Flat Glass Group (FGG 6865.HK, 601865.CH) also echoed such upbeat observations. The company had earlier made a voluntary announcement indicating strong orders for its solar glass products in 2M22, particularly for distributed solar applications. In the latest results briefing, FGG disclosed it currently holds only c.7%-10% of inventory, indicating fast product turnover. Government statistics corroborate the optimism regarding solar component demand. New solar installations in China are off to a good start in 2022, despite high polysilicon prices. In 2M22, NEA reported 10.86GW of new solar installations in China, up 234% y-o-y. Strong demand is also observed in overseas markets. General Administration of China (GACC) statistics show the export value of solar cells from China surging 108.8% y-o-y in 2021.

Omicron disruption to production minimal. Since Mar-22, China has been battling a spike in COVID-19 Omicron variant infections. However, our channel checks with solar component manufacturers indicate the latest wave of infections minimally impacted production. Several factors helped mitigate the situation. First, the spread of the virus is concentrated in Shanghai. Provinces with major polysilicon production capacity such as Sichuan, Xinjiang, and Inner Mongolia each have recorded <50 confirmed daily cases in the past two weeks. Second, solar component companies have implemented “closed-loop” management at their plants to maintain production. Under such arrangements, workers sleep, live, and work on factory premises, and thereby avoid getting infected from outside.

Logistics a wildcard but policy support emerging. While solar component production was minimally affected by Omicron, the transportation of goods remains challenging. Our channels checks indicate deliveries have been delayed as...
The Port of Shanghai remains congested, which mostly impacts export markets. Solar component manufacturers had to redirect their export orders to other ports. In response, China's officials have pledged to disentangle the transport network. On 11 April, the State Council issued a directive on freight transport, forbidding the shutdown of highways, railway stations, and airports without permission. Similar announcements were made by other government agencies including the NDRC, Ministry of Commerce (MOFCOM), Civil Aviation Administration, and the National Railway Administration. Further easing of pandemic restrictions on the transport sector should help solar components reach their destinations, thereby facilitating installations. Historically, most solar installations are completed near the end of the calendar year. We expect the temporary disruption to truck transport to be resolved in 2H22. Therefore, we maintain our latest solar installation forecast of c.75 GW for China in 2022, up 36% y-o-y.

We like LONGi (601012.CH) and Flat Glass (6865.HK, 601865.CH). With new polysilicon supply coming to the market, a key bottleneck for solar installations is removed. As downstream solar operators expand their generation capacity in 2H22-23, demand for solar components should benefit. This should help drive the sales volume of solar component manufacturers such as LONGi and Flat Glass.

Maintain BUY on LONGi with target price of Rmb95. LONGi's pricing power remains intact, as evidenced by the company's price hikes for its various wafer models since mid-Jan. In late Mar-22, the company raised ASPs across all its wafer products by 1.8%-1.9%. LONGi planned to expand its solar/wafer module production capacity to 105GW/65GW at end-2021, up 24%/30% y-o-y. The resolution of the polysilicon bottleneck should help LONGi ramp up the utilization rate of its new production capacity, driving sales volume growth. Currently, LONGi's shares trade at c.21x FY22 PE, near 2SD below the historical average of c.31x since Sep-2020. Our target price of Rmb95 is based on a target PEG of 1.2x.

Maintain BUY on Flat Glass Group H-shares (6865.HK) and HOLD on A-shares (601865.CH). FGG should also benefit from solid demand. FGG H-shares currently trades at c.17x FY22 PE, more than 1SD below the historical average of c.21.5x since Sep-20. FGG plans to achieve 20,600 tons/day of glass production capacity by end-2022, up 68% y-o-y. Resolution of the polysilicon bottleneck should help drive demand for modules, of which FGG's solar glass is a key component. We recommend BUY on FGG H-shares and HOLD on A-shares. Based on a target PEG of 1x, we derive a TP of HK$45.0 for FGG's H-shares. Our A-share TP is Rmb53.

Source: Thomson Reuters, DBS HK
Industry Focus
China Renewable Sector (Solar)

**Flat Glass – H-share PE valuation**

![Graph showing PE valuation for Flat Glass H-share with key points at Avg: 21.4x, +1SD: 25.7x, -1SD: 17.1x, +2SD: 30x, -2SD: 12.8x.]

Source: Thomson Reuters, DBS HK

**Flat Glass – A-share PE valuation**

![Graph showing PE valuation for Flat Glass A-share with key points at Avg: 35.1x, +1SD: 41.2x, -1SD: 29x, +2SD: 47.4x, -2SD: 22.9x.]

Source: Thomson Reuters, DBS HK
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China Renewable Sector (Solar)

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*Share price appreciation + dividends

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China Renewable Sector (Solar)

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