



Company Report: Beijing Enterprises Water (00371 HK)

公司报告: 北控水务 (00371 HK)

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Fast Expansion Continued, Upgrade to "Buy" 快速扩张持续, 调高至 "买入"

- **BEWG (00371 HK) 2014 revenue increased 39% YoY to HKD6,407 million. Net profit increased 65% YoY to HKD1,794 million. Results were better than expectation, mainly because of higher than expected increase in other income.** Gross margin increased 0.1 pts YoY to 39.2%. As at 31 Dec 2014, total borrowings were up 22% YoY to HKD23,490 million. Net gearing was up 4.2 pts YoY to 90.7%.
- Total daily design capacity was up 22% YoY to 20.2 million tons as at 31 Dec 2014, of which 4.7 million tons were new. Capacity expansion was much faster than expected. With the release of new capacity, we expect sewage and reclaimed water treatment services and water distribution services to first overtake construction services as the main revenue contributor starting 2015. **We expect overall revenue to increase at a CAGR of 28.3% and gross margin to increase from 39.2% to 41.8% in 2014-2017. In addition, we think the Company might require financing new projects with more equity financing.**
- Raise EPS estimates for FY15-16 by 5.1% and 8.9% to HKD0.250 and HKD0.336 respectively, and initiate that of FY17 at HKD0.449. **We think current valuation of 21.9x/16.3x/12.2x FY15/16/17 PER is undervalued. Raise the TP to HKD7.50, representing 30.0x/22.3x/16.7x FY15/16/17 PER. Upgrade to "Buy".**
- 北控水务(00371 HK) 2014 年营业收入同比增 39%至 64.07 亿元(港元, 下同)。纯利同比增 65%至 17.94 亿元。业绩优于预期。主要因为其它收入增长高于预期。毛利率同比增 0.1 个百分点至 39.2%。截至 2014 年 12 月 31 日, 总借贷同比增 22%至 234.90 亿元。净债务比率提高 4.2 个百分点至 90.7%。
- 截至 2014 年 12 月 31 日, 总日均设计处理量为 20.2 百万吨, 同比增 22%。其中新增处理量为 4.7 百万吨。公司产能的增长远高于预期。随着产能释放, 我们预计公司的污水处理及再生水处理服务收入, 以及供水服务收入将于 2015 年首次超过建造收入成为收入最大来源。于 2014 至 2017 年间, 预计总收入的年复合增长率为 28.3%, 毛利率则可从 39.2% 提高至 41.8%。此外, 公司或透过更多股权融资支持新项目。
- 上调 2015-2016 年每股盈利预测 5.1%和 8.9%, 分别至 0.250 港元和 0.336 港元, 及首次提供 2017 年每股盈利预测 0.449 港元。我们认为当前的估值 21.9/16.3/12.2 倍 2015/2016/2017 年预期市盈率是低估, 调高其目标价至 7.50 港元, 对应 30.0/22.3/16.7 倍 2015/2016/2017 年预期市盈率。上调至 "买入"。

Rating:

Buy

Upgraded

评级:

买入 (上调)

6-18m TP 目标价:

HK\$7.50

Revised from 原目标价:

HK\$6.38

Share price 股价:

HK\$5.480

Stock performance

股价表现



Change in Share Price 股价变动	1 M 1 个月	3 M 3 个月	1 Y 1 年
Abs. % 绝对变动 %	20.2	15.4	22.2
Rel. % to HS index 相对恒指变动 %	15.1	6.6	7.2
Avg. share price(HK\$) 平均股价 (港元)	5.0	4.9	5.1

Source: Bloomberg, Guotai Junan International.

Year End 年结 12/31	Turnover 收入 (HKD m)	Net Profit 股东净利 (HKD m)	EPS 每股净利 (HKD)	EPS 每股净利变动 (Δ%)	PER 市盈率 (x)	BPS 每股净资产 (HKD)	PBR 市净率 (x)	DPS 每股股息 (HKD)	Yield 股息率 (%)	ROE 净资产收益率 (%)
2013A	6,406	1,084	0.140	28.7	39.2	1.576	3.5	0.052	0.9	10.0
2014A	8,926	1,794	0.208	48.5	26.4	1.813	3.0	0.078	1.4	12.3
2015F	11,856	2,165	0.250	20.5	21.9	2.061	2.7	0.088	1.6	12.8
2016F	15,030	2,907	0.336	34.3	16.3	2.395	2.3	0.118	2.1	15.0
2017F	18,866	3,883	0.449	33.6	12.2	2.841	1.9	0.157	2.9	17.0

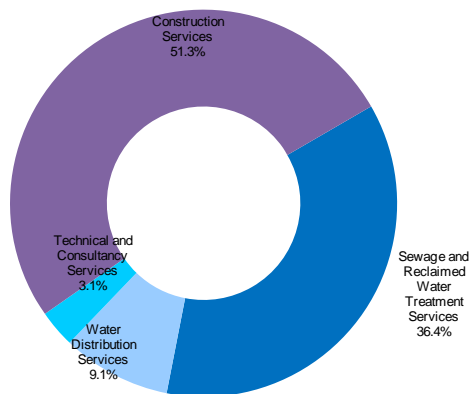
Shares in issue (m) 总股数 (m)	8,707.4	Major shareholder 大股东	BEHL	43.9%
Market cap. (HK\$ m) 市值 (HK\$ m)	47,716.6	Free float (%) 自由流通比率 (%)		56.1
3 month average vol. 3 个月平均成交股数 ('000)	27,228.6	FY15 Net gearing (%) FY15 净负债/股东资金 (%)		99.0
52 Weeks high/low (HK\$) 52 周高/低	6.150 / 4.090	FY14-17 EPS CAGR 14-17 年每股盈利复合年增长率 (%)		29.3

Source: the Company, Guotai Junan International.

2014 net profit increased 65% YoY to HKD1,794 million. Results were better than expected. BEWG (00371 HK) 2014 revenue increased 39% YoY to HKD6,407 million. Net profit increased 65% YoY to HKD1,794 million. Results were better than expected. The higher than expected results were mainly due to the increase in other income and gain by a triple in other income and gain to HKD608 million (HKD101 million from gain on sales of land and HKD95 million from foreign exchange gain). Gross margin increased 0.1 ppts YoY to 39.2%. Administrative expenses were up 37% YoY to HKD1,066 million due to the fast expansion in businesses. Finance costs were up 38% YoY to HKD1,084 million due to increase in borrowings size and slight increase in interest rate. As at 31 Dec 2014, total borrowings were HKD23,490 million, up 22% YoY. Net gearing was 90.7%, up 4.2 ppts YoY.

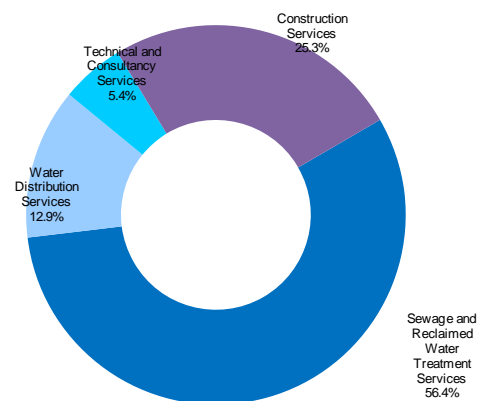
Capacity expansion faster than expected, sewage and reclaimed water treatment services revenue should overtake construction services to be the largest contributor in 2015. As at 31 Dec 2014, BEWG had a total of 326 water plants, which included 250 sewage treatment plants, 69 water distribution plants, 6 reclaimed water treatment plants, and 1 seawater desalination plant. Total daily design capacity was 20,150,050 tons, up 21% YoY. Total daily design capacity for new projects secured for the year was 4,651,900 tons, consisting of 1,944,200 tons of BOT, 283,500 tons of TOT, 228,000 tons of DBOO, 900,000 tons of PPP, 510,200 tons of entrustment operation and 786,000 tons through M&A. Increase in capacity was much higher than the original target of 3.5 million tons/day. Due to the fast release in capacity, both sewage and reclaimed water treatment services revenue and water distribution services revenue increased substantially (up 51.8% YoY and 111.8% YoY respectively). We expect sewage and reclaimed water treatment services revenue (2015 estimate: HKD5,200 million) can first overtake that of construction services (2015 estimate: HKD5,000 million) to be the largest revenue contributor.

Fig 1: 2014 Segmental Revenue



Source: the Company.

Fig 2: 2014 Segmental Gross Profit



Source: the Company.

We expect a CAGR of 28.3% for the revenue during 2014-2017. Although the base seemed high, we think the Company still has a lot of growth potential. Firstly, the Company expected to increase daily design capacity to 40 million tons within 4 to 5 years, doubling the current level. Secondly, only 54% of the Company's treatment plants reached 1A treatment standard, 45% were 1B and 1% was 2A. With the gradual upgrade for the 46% plants, water treatment tariff can be raised accordingly. Thirdly, normal adjustment of tariff of existing plants. During 2014, tariff of 12 plants were raised on average of 13.8%. Given these, we think revenue can maintain a fast growth in the next three years, with a CAGR of 28.3%.

Gross margin to increase from 40.8% to 41.8% in 2015-2017. Overall gross margin increased 0.1 ppts YoY to 39.2%, despite a sharp decrease in gross margin of sewage and reclaimed water treatment services. This was because sewage and reclaimed water treatment services gross margin was much higher than overall gross margin, and its revenue contribution increased substantially during the year with fast expansion in capacity. In addition, gross margin of water distribution increased 3.0 ppts YoY. We expect sewage and reclaimed water treatment services gross margin to further decline but that

should still remain above 60%. Moreover, water distribution services gross margin should also remain above 50%. As both of their gross margins remain higher than overall gross margin and their revenue contribution should increase further, we expect overall gross margin to rise gradually from 40.8% in 2015 to 41.8% in 2017.

Table 1: 2014 Segmental Performance Summary

HKD million	Revenue	Growth	Gross Profit	Growth	Gross Margin	YoY
Sewage and Reclaimed Water Treatment	3,250	+51.8%	2,050	+33.8%	63.1%	-8.4 ppts
Construction Services	4,583	+21.7%	921	+22.4%	20.1%	+0.1 ppts
Water Distribution	813	+111.8%	467	+123.6%	57.4%	+3.0 ppts
Technical and Consultancy Services	281	+138.7%	196	+95.5%	69.8%	-15.5 ppts
Less: Operating Concessions Amortization			(137)	+57.6%		
Total	8,926	+39.3%	3,496	+39.5%	39.2%	+0.1 ppts

Source: the Company.

Further equity financing should be coming. According to the current expansion pace, the Company should spend HKD7 billion to HKD8 billion in capital expenditure annually. Start 2015, we estimate that the Company's operating cash inflow should reach at least HKD4 billion annually, excluding approximately HKD1 billion for dividends payout and other expenditures, the Company should have at least HKD3 billion free cash for investment. That is, the Company at most has to borrow HKD5 billion for building/acquiring new projects. This translates to a capital structure of 62.5% of debt of its new projects (HKD5 billion / HKD8 billion), which is similar to the Company's current capital structure (debt ratio 63.0% as at 2014). Interest coverage should remain above 3x (3.2x for FY14). We think these suggest that even if the Company does not finance through equity in the coming 3 years, it can still maintain debt ratio below 70%. However, this appears a bit tight, especially net gearing should easily go through 100% (90.7% as at 2014) with just 1 more year of new investment financed purely by debt. Hence, we still expect the Company to do equity financing within 3 years.

Raise the TP to HKD7.50, Upgrade to "Buy". Raise EPS estimates for FY15-16 by 5.1% and 8.9% respectively to HKD0.250 and HKD0.336, and initiate the EPS estimate of FY17 at HKD0.449. The Company has continued to deliver higher than expected results and we think the coming 3 years is another high growth period for the Company. On the back of "Water Ten" policy being released very soon, the Company, being the largest sewage and reclaimed water treatment services company in China, should benefit substantially from such. Moreover, the encouragement of the use of "PPP" to invest in sewage treatment projects bring large opportunities to SOEs (work well with the authority and the local governments) with private management (high efficiency), such as the Company. Its current valuation is at 21.9x/16.3x/12.2x FY15/16/17 PER, clearly underestimating the Company's growth potential. Raise the TP to HKD7.50, representing 30.0x/22.3x/16.7x FY15/16/17 PER. Upgrade to "Buy".

Company Rating Definition

The Benchmark: Hong Kong Hang Seng Index

Time Horizon: 6 to 18 months

Rating	Definition
Buy	Relative Performance >15%; or the fundamental outlook of the company or sector is favorable.
Accumulate	Relative Performance is 5% to 15%; or the fundamental outlook of the company or sector is favorable.
Neutral	Relative Performance is -5% to 5%; or the fundamental outlook of the company or sector is neutral.
Reduce	Relative Performance is -5% to -15%; or the fundamental outlook of the company or sector is unfavorable.
Sell	Relative Performance <-15%; or the fundamental outlook of the company or sector is unfavorable.

Sector Rating Definition

The Benchmark: Hong Kong Hang Seng Index

Time Horizon: 6 to 18 months

Rating	Definition
Outperform	Relative Performance >5%; or the fundamental outlook of the sector is favorable.
Neutral	Relative Performance is -5% to 5%; or the fundamental outlook of the sector is neutral.
Underperform	Relative Performance <-5%; or the fundamental outlook of the sector is unfavorable.

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