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HONG KONG RESEARCH
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Analyst: Paul Sham

CLP HOLDINGS LIMITED (中電控股)

Sector	: Utilities	Chairman	: The Hon. Sir Michael Kadoorie
HKSE Code	: 00002		
Market Price	: HK$68.55 (02/03/2015)	CEO	: Mr. Richard Lancaster
Shares Issued	: 2,526.45m		
Mkt. Cap.	: HK$173,188m	CFO	: Mr. Geert Peeters
52 weeks Hi/ Lo	: HK$69.85 / HK$56.0		
HSI	: 24,887.44 (02/03/2015)		
Main Business	: Electricity generation		

SUMMARY OF THE FINAL RESULTS FOR THE YEAR ENDED 31ST DECEMBER 2014

Final Results Highlights

	FY2014	FY2013	
	HK$ million	HK$ million	*Change*
Revenue	92,259	104,530	*-11.7%*
Operating earnings from energy activities	10,684	9,756	*+9.5%*
Other earnings and unallocated costs	(622)	(449)	*+38.5%*
One-off items	1,159	(3,247)	*-135.7%*
Profit attributable to shareholders	**11,221**	**6,060**	***+85.2%***
	HK$	HK$	
Basic EPS	4.44	2.40	*+85.0%*
Final DPS	1.00	0.98	*+2.0%*
Total DPS	2.62	2.57	*+1.9%*
	As of 31st Dec 2014	**As of 31st Dec 2013**	
Net debt to equity ratio	71.6%	58.2%	

- CLP Holdings ("CLP") reported FY14 net profit of HK$11,221m, up 85.2% y-o-y. The results were better than the consensus estimates of HK$10,853m. Operating earnings from energy activities rose 9.5% y-o-y to HK$10,684m, driven by the increased stake in the HK power business starting May 2014 and lower depreciation expense in Australia.
- The discrepancy between growth in reported net profit and core earnings was attributable to some major one-off items, including: 1) impairment charges of HK$3,106m due to projected lower wholesale electricity prices in Australia in FY13; 2) one-off gain of HK$1,953m from the acquisition of the further 30% interest in Castle Peak Power Company (CAPCO) and the 51% interest in Hong Kong Pumped Storage Development Company (PSDC) in FY14; and 3) impairment of HK$1,578m arising from reduction in coal reserves in Australia and net tax credit of HK$545m relating to settlement of outstanding matters with the Australian Taxation Office in FY14.
- Thanks to the 9.5% y-o-y growth in operating earnings, CLP raised the 4th interim dividend by 2.0% y-o-y to HK$1.00 per share. Total dividend per share for 2014 was HK$2.62, up from HK$2.57 a year ago.
- As of 31st December 2014, CLP's cash and cash equivalent fell to HK$4,393m, down from HK$5,233m a year earlier. Total borrowing rose to HK$67,435m from HK$56,051m during the same period. As a result, its net debt to equity ratio surged to 71.6% from 58.2% y-o-y.

Business Review

- Earnings breakdown by business segments:

	FY2014 HK$ million	FY2013 HK$ million	Change
Hong Kong / Hong Kong related	**7,782**	**7,074**	***+10.0%***
Local electricity business	7,777	6,966	*+11.6%*
PSDC and sales to Guangdong from HK	71	125	*-43.2%*
Other activities	(66)	(17)	*+288.2%*
Overseas	**2,902**	**2,682**	***+8.2%***
Mainland China	1,579	2,131	*-25.9%*
Australia	756	126	*+500.0%*
India	270	184	*+46.7%*
Southeast Asia & Taiwan	297	241	*+23.2%*
Other earnings	**(622)**	**(449)**	***+38.5%***
Operating earnings	*10,062*	*9,307*	*+8.1%*
Non-recurring items	1,159	(3,247)	
Attributable profit to shareholders	11,221	6,060	*+85.2%*

- Earnings from the **Hong Kong** recorded a 10.0% y-o-y growth to HK$7,782m, attributable to the additional earnings following the completion of the acquisition of CAPCO's 30% stake in May 2014, and the increased permitted return from a higher level of average net fixed assets.

- Even though coal-fired projects were benefited from lower coal prices in FY14, earnings contribution from **China** power business dropped 25.9% y-o-y to HK$1,579m in 2014. The decline in earnings was mainly due to 1) no profit sharing for FY2014 under the Share Transfer Agreement of CSEC Guohua and Shenmu (coal-fired projects) disposal; 2) lower profits from Fangchenggang (a coal-fired power plant) as a result of lower electricity sold and expiry of an income tax credit; and 3) reduced earnings from renewable projects amid lower water flows and poor wind resources.

- Earnings from the **Australia** business rebounded strongly by 500% in FY14 to HK$756m, after falling 92.5% y-o-y in 2013. The rise in earnings was attributed to lower depreciation and amortisation on reduced asset bases after the 2013 impairment, decreased finance costs resulting from lower interest rates, and lower bad debt provision.

- **Indian** business reported net profit of HK$270m, up 46.7% y-o-y, due to improved performance from Jhajjar (a 1,320MW coal-fired power plant) as a result of improved coal supplies. Earnings from Paguthan and wind projects remained at similar levels as in 2013.

- Operating earnings in **Southeast Asia and Taiwan** recorded higher earnings in 2014, up 23.2% y-o-y to HK$297m. Earnings from Ho-Ping (1.32GW power plant) were higher mainly because in 2013 there was a one-off provision (HK$60m) for a penalty imposed by the Taiwan Fair Trade Commission. Excluding the one-off provision, underlying profit should be largely flat y-o-y. On the other hand, earnings from Lopburi solar project in Thailand improved due to the commissioning of an 8MW expansion in May 2013 and higher solar irradiance.

Outlook & Prospect

- ***Stable SOC earnings till 2018*** CLP's net tariff increased by 3.1% y-o-y to HK$1.142/kWh starting 2015, of which the basic tariff dropped 1.4% y-o-y to HK$0.872/kWh, while the fuel clause charge increased substantially, by 20.5% y-o-y, to HK$0.27/kWh to reflect higher fuel costs for doubling in natural gas usage in order to meet the emission target. Nevertheless, no direct earnings impact from tariff adjustment, as earnings derived from the Hong Kong power business are protected by the Scheme of Control (SoC), which allows power companies to earn a permitted return (9.99% for regular SoC fixed assets) till 2018. The government may discuss with the two electric utilities prior to 1st January 2016 regarding potential changes to the electricity supply framework and transitional issues after 2018. There could be downside risk to the 9.99% return on net fixed assets after 2018 as the sharp tariff hike in recent years by CLP had already created certain social dissatisfaction on its SoC business.

- ***Outlook in Australia remains challenging*** Management believes the 2015 outlook in Australia will remain challenging with aggressive retail competition and overcapacity of electricity supply. Although CLP is on track to merge EnergyAustralia's two billing systems starting December 2014, which will allow the company to save A$100m in operating expense per annum, the cost saving will be offset by the y-o-y depreciation of AUD against USD (down 12.7% in 2H14) as well as the absence of carbon tax compensation in 2015 (~HK$400m in 2014). Therefore, we believe earnings growth will likely be mild in 2015 and more meaningful improvement in earnings will only happen in 2016.

- ***China operations on track*** In respect of China operation, the solar project in Jinchang in Gansu Province (85MW, 51% owned by CLP) has been affected by grid curtailment because of the commissioning of other thermal and solar power plants in the region and flat local demand. It may drag China's power business slightly in 2015. Nevertheless, project pipeline remains strong as Fangchenggang Phase II (2x660MW) had commenced construction and 4 wind projects will start the construction in 2015.

- ***Valuation*** Trading at 16.3x FY15E P/E, CLP's valuation looks expensive. We prefer PAH over CLP given the potential earnings upside from any sizeable M&A on the back of PAH's ample cash reserve or the paying out of special dividends. The performance of CLP is expected to lag behind PAH to reflect the combination of sluggish business performance in Australia as well as its larger HK exposure, which will face potential uncertainty in its Hong Kong SoC return after 2018. The possible interest rate hike may also curb market attention on CLP's 3.9% 2015E dividend yield (vs PAH's 3.3%).

Recommendation: *Prefer Power Assets*

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