

JPM-pp1

Asia Pacific Equity Research

16 March 2015

# Sound Global Limited (967 HK)

## Neutral

Price: HK\$7.00

16 Mar 2015

Price Target: HK\$7.10

PT End Date: 31 Dec 2015

### Shares likely to stay suspended until April

Sound Global shares will continue to be suspended until its 2014 results are announced, likely in April, in our view. We believe the two key things to watch for in the near term are: 1) whether the shares will resume trading on or before 9 Apr (as this will mark the maximum 15 days of suspension allowed under the asset injection agreement) and 2) whether annual net profit growth in 2014 will still be 35-42% as disclosed in the profit alert on 2 Feb. We remain Neutral on Sound Global and prefer China Everbright Int'l in the China water sector.

*Sound Global held a conference call today to further explain reasons for the delay in the results announcement. Please see below for our key takeaways from the call.*

- **Delay due to more stringent guidelines and increased workload for auditor.** Sound Global management said the results announcement was delayed because its auditor, Deloitte, had placed more stringent auditing guidelines after questions were raised on the company's financials from an independent research report published in February. In addition, the auditor's workload had increased due to the preparation of the three clarification statements made in Feb 2015. Management reiterated that daily business operations remain normal and that there was no impact on the progress of BOT projects and no cancellation on EPC orders.
- **Results announcement unlikely before 31 Mar.** Management said they will continue to communicate closely with Deloitte, but they stopped short of saying when the results would be announced, only that it was unlikely to be issued before 31 Mar, as per the auditor's estimate.
- **Asset injection may not complete if shares are suspended for >15 days.** As per the agreement signed between Sound Global and Sound Environmental, one of the conditions precedent for this asset injection is that Sound Global shares are not suspended for more than 15 consecutive trading days. Management said the transaction with Sound Environmental may terminate if that were to happen. Resumption of trading on 9 April or earlier would be fewer than 15 consecutive days, on our estimates. We believe a potential termination of the asset injection may be a negative in the long run because this would have allowed Sound Global to grow its recurring earnings base faster.
- **Profit alert based on company's preliminary assessment.** Management said the profit alert guiding 2014 net profit growth of 35%-42% was based on the company's preliminary assessment. We believe this along with any statements made from the auditor would be some of the key items to watch for in the results announcement.

### Investment Thesis

Sound Global (SGL) constructs and operates wastewater treatment and water recycling plants. It has an equipment manufacturing arm and an R&D division, capable of customizing products for customers. The company was founded by Wen Yibo, a former Tsinghua University lecturer of environmental engineering and water industry veteran, who started his first water equipment company with his wife in 1993. Mr Wen is also the majority shareholder of Sound Environmental (000826 CH), a China-listed company involved in waste-to-energy and wastewater treatment business.

### Valuation

Our Dec-15 PT is based on an historical average P/E multiple of 11x on 2015 EPS. Its historical trading band is 6-16x P/E. Our PT implies a 35% discount to our DCF-derived valuation of HK\$10.8 and 11x 2015 P/E, 1.7x 2015 P/B.

### Risks to Rating and Price Target

Downside risks to our Neutral rating and price target include fewer-than-expected new project wins, lower-than-expected margins from rural wastewater treatment projects and the accumulation of accounts receivable.

Upside risks include a stronger-than-expected recovery in investor confidence in the name and a higher-than-expected number of new project wins.

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## Other Companies Discussed in This Report (all prices in this report as of market close on 16 March 2015)

China Everbright International (0257.HK/HK\$11.42/Overweight)

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Date	Rating	Share Price (HK\$)	Price Target (HK\$)
11-Feb-14	N	7.69	9.00
25-Apr-14	OW	7.38	9.00
20-Aug-14	OW	7.87	9.90
09-Oct-14	OW	8.21	11.00
15-Feb-15	N	5.39	7.10

<http://gps-app.emea.jpmchase.net:6080/server/console/chart/?shareClassId=500216&shareClassServerId=4&chartDesignation=1&actionType=C>

Date	Rating	Share Price (HK\$)	Price Target (HK\$)
21-Oct-11	N	1.83	2.30
21-Feb-12	N	3.53	3.90
05-Jun-12	OW	3.46	4.50
23-Aug-12	OW	4.15	4.80
07-Nov-12	OW	3.86	4.60
28-Feb-13	OW	4.99	5.30
11-Jul-13	OW	6.08	7.60
06-Aug-13	OW	7.02	8.30
24-Apr-14	OW	10.36	13.00

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\*Percentage of investment banking clients in each rating category.

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