Deutsche Bank
Markets Research

Rating
Sell

Asia
Hong Kong

Utilities
Utilities

Company
Hong Kong & China Gas

Reuters	Bloomberg	Exchange	Ticker
0003.HK	3 HK	HKG	0003
ADR Ticker	ISIN		
HOKCY	US4385503036		

Date
19 March 2015

Recommendation Change

Price at 18 Mar 2015 (HKD)	17.48
Price target - 12mth (HKD)	15.00
52-week range (HKD)	18.82 - 14.32
HANG SENG INDEX	23,901

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Downgrading to Sell

Double hit in 2015; downgrading to Sell
Weak earnings growth of only 6% in 2015E (from 13% CAGR in 2009-14) and a high 25x PE could trigger a de-rating of HKG and combine to justify our downgrade to Sell. The premium valuation was helped in the past by strong growth in mainland gas business but now could be eroded by poor results in its new energy division (where HKG lacks expertise), especially after the sharp drop in oil and commodity prices. The company also faces increased competitive pressure on its China gas business as other fuels are now much cheaper. This report marks the transfer of coverage from Michael Tong to Yuxiao Peng.

New energy business: a challenging year in 2015 on lower oil price
HKG's FY14 core earnings were 2% below our forecast, mainly on weak results from the new energy segment (-2% yoy). This segment, which includes oil E&P, coal mines and coal-to-methanol projects, could face another c.20% earnings decline in 2015, with a c.40% drop in oil price, c.30% drop in methanol price, and c.10% decline in coal price over the past year. This segment accounted for nearly 20% of HKG's total assets but only 7% of its net profit in 2014. Such exposure could grow further as the majority of HKG's capex is allocated to this segment, bringing higher risk and volatility.

Mainland gas business: economic disadvantage poses risks
We estimate the natural gas price to be at a premium of 13% over LPG and 67% over fuel oil, even after the modest gas price cut of 2.7% (blended basis) effective from 1 April 2015. The pricing disadvantage, in a weak macro outlook, is putting pressure on HKG's city gas business in China. We still assume 12% yoy volume growth and a stable gross margin of Rmb0.67/cum in 2015. But every 1% lower volume or Rmb0.01/cum margin squeeze could have 0.8% and 1.1% earnings downside, respectively, for the company.

SOTP target price of HK$15.0; Sell
Our SOTP target price of HK$15.0 comprises HK$7.0 from the HK gas segment, HK$5.3 from mainland China gas, HK$1.0 from new energy, and the rest from property and others. Upside risks: better-than-expected results from the new energy business, value-accretive M&A, higher-than-expected gas sales volume, a further cut in gas cost, and share buybacks by the company.

Key changes

Rating	Hold to Sell	↓	
Price target	17.20 to 15.00	↓	-12.8%
Sales (FYE)	41,026 to 34,133	↓	-16.8%
Op prof margin (FYE)	24.5 to 21.2	↓	-13.3%
Net profit (FYE)	7,742.5 to 7,377.6	↓	-4.7%

Source: Deutsche Bank

Price/price relative

Performance (%)	1m	3m	12m
Absolute	-0.1	2.2	17.5
HANG SENG INDEX	-3.7	4.7	10.7

Source: Deutsche Bank

Forecasts And Ratios

Year End Dec 31	2013A	2014A	2015E	2016E	2017E
Sales (HKDm)	28,246	31,615	34,133	37,016	39,758
Reported NPAT (HKDm)	6,854	7,109	7,378	8,037	8,450
DB EPS FD (HKD)	0.601	0.662	0.702	0.765	0.804
DB EPS growth (%)	10.9	10.1	6.0	8.9	5.1
PER (x)	28.6	25.1	24.9	22.9	21.7
Price/BV (x)	3.4	3.5	3.3	3.1	2.9
DPS (net) (HKD)	0.318	0.350	0.385	0.424	0.466
Yield (net) (%)	1.9	2.1	2.2	2.4	2.7
ROE (%)	14.4	13.9	13.6	13.8	13.6

Source: Deutsche Bank estimates, company data

Model updated:18 March 2015

Running the numbers

Asia

Hong Kong

Utilities

Hong Kong & China Gas

Reuters: 0003.HK | Bloomberg: 3 HK

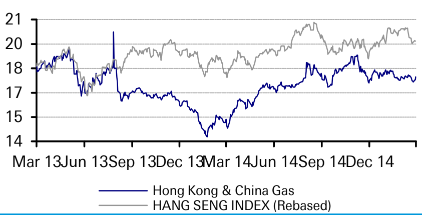
Sell

Price (18 Mar 15)	HKD 17.48
Target Price	HKD 15.00
52 Week range	HKD 14.32 - 18.82
Market Cap (m)	HKDm 183,813
	USDm 23,675

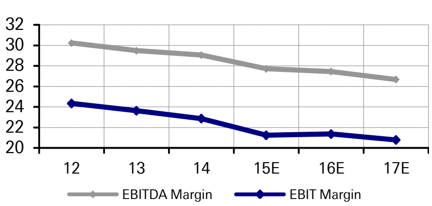
Company Profile

The bulk of HKG's earnings come from a vertically integrated gas distribution business which involves the production and distribution of towngas to 1.7m customers in Hong Kong. Returns/tariffs from HKG's Hong Kong based gas business are not regulated. HKG has also been building a portfolio of stakes in city gas JVs located in mainland China and is keen to invest in the upstream gas sector, water and the environmental-friendly energy businesses. Additionally, HKG has some property investments in Hong Kong.

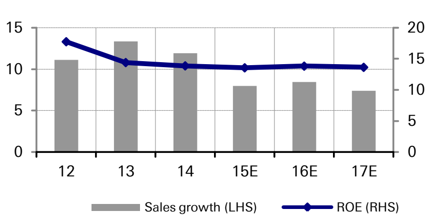
Price Performance



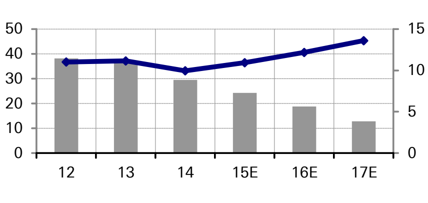
Margin Trends



Growth & Profitability



Solvency



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Fiscal year end 31-Dec	2012	2013	2014	2015E	2016E	2017E
Financial Summary						
DB EPS (HKD)	0.54	0.60	0.66	0.70	0.76	0.80
Reported EPS (HKD)	0.73	0.65	0.68	0.70	0.76	0.80
DPS (HKD)	0.29	0.32	0.35	0.39	0.42	0.47
BVPS (HKD)	4.3	4.7	5.0	5.3	5.7	6.1
Weighted average shares (m)	10,516	10,516	10,515	10,512	10,512	10,512
Average market cap (HKDm)	152,315	180,806	174,777	183,813	183,813	183,813
Enterprise value (HKDm)	113,824	140,401	134,831	140,092	135,621	130,311
Valuation Metrics						
P/E (DB) (x)	26.7	28.6	25.1	24.9	22.9	21.7
P/E (Reported) (x)	19.8	26.4	24.6	24.9	22.9	21.7
P/BV (x)	3.94	3.37	3.55	3.27	3.06	2.88
FCF Yield (%)	nm	0.5	0.7	2.1	2.5	3.1
Dividend Yield (%)	2.0	1.9	2.1	2.2	2.4	2.7
EV/Sales (x)	4.6	5.0	4.3	4.1	3.7	3.3
EV/EBITDA (x)	15.1	16.9	14.7	14.8	13.3	12.3
EV/EBIT (x)	18.8	21.0	18.6	19.3	17.1	15.8
Income Statement (HKDm)						
Sales revenue	24,923	28,246	31,615	34,133	37,016	39,758
Gross profit	7,553	8,349	9,213	9,485	10,191	10,637
EBITDA	7,533	8,327	9,184	9,459	10,163	10,608
Depreciation	1,465	1,649	1,952	2,207	2,255	2,339
Amortisation	0	0	0	0	0	0
EBIT	6,067	6,677	7,233	7,253	7,908	8,269
Net interest income(expense)	-551	-599	-726	-663	-650	-608
Associates/affiliates	3,655	2,672	3,215	3,202	3,432	3,623
Exceptionals/extraordinaries	449	27	-32	0	0	0
Other pre-tax income/(expense)	265	633	185	384	385	386
Profit before tax	6,231	6,739	6,660	6,973	7,643	8,047
Income tax expense	1,485	1,655	1,771	1,796	1,964	2,077
Minorities	689	902	892	889	964	1,032
Other post-tax income/(expense)	0	0	-102	-112	-112	-112
Net profit	7,712	6,854	7,109	7,378	8,037	8,450
DB adjustments (including dilution)	-2,012	-534	-149	0	0	0
DB Net profit	5,700	6,320	6,960	7,378	8,037	8,450
Cash Flow (HKDm)						
Cash flow from operations	5,876	6,112	7,268	7,376	7,838	8,240
Net Capex	-5,906	-5,294	-6,127	-3,557	-3,190	-2,511
Free cash flow	-29	818	1,141	3,819	4,648	5,728
Equity raised/(bought back)	0	0	0	0	0	0
Dividends paid	-4,243	-3,146	-3,461	-3,806	-4,186	-4,605
Net inc/(dec) in borrowings	6,234	-1,050	0	0	0	0
Other investing/financing cash flows	-1,020	-39	4,887	2,207	2,336	2,460
Net cash flow	943	-3,417	2,568	2,220	2,797	3,583
Change in working capital	*535*	*-51*	*362*	*260*	*81*	*117*
Balance Sheet (HKDm)						
Cash and other liquid assets	12,448	10,138	13,156	15,376	18,173	21,756
Tangible fixed assets	41,914	47,002	51,354	52,880	53,990	54,339
Goodwill/intangible assets	0	0	0	0	0	0
Associates/investments	36,568	39,658	39,960	41,137	42,407	43,730
Other assets	8,094	9,597	9,942	10,742	11,501	12,216
Total assets	99,024	106,395	114,411	120,135	126,071	132,042
Interest bearing debt	31,721	30,623	31,534	31,534	31,534	31,534
Other liabilities	16,836	19,401	20,653	22,005	23,226	24,431
Total liabilities	48,557	50,025	52,187	53,539	54,760	55,965
Shareholders' equity	45,319	49,868	52,628	56,200	60,050	63,895
Minorities	5,148	6,503	9,596	10,396	11,261	12,182
Total shareholders' equity	50,467	56,371	62,224	66,596	71,311	76,077
Net debt	*19,273*	*20,485*	*18,378*	*16,158*	*13,361*	*9,778*
Key Company Metrics						
Sales growth (%)	11.1	13.3	11.9	8.0	8.4	7.4
DB EPS growth (%)	9.6	10.9	10.1	6.0	8.9	5.1
EBITDA Margin (%)	30.2	29.5	29.1	27.7	27.5	26.7
EBIT Margin (%)	24.3	23.6	22.9	21.2	21.4	20.8
Payout ratio (%)	39.4	48.8	51.8	54.9	55.4	58.0
ROE (%)	17.7	14.4	13.9	13.6	13.8	13.6
Capex/sales (%)	23.7	18.7	19.4	10.4	8.6	6.3
Capex/depreciation (x)	4.0	3.2	3.1	1.6	1.4	1.1
Net debt/equity (%)	38.2	36.3	29.5	24.3	18.7	12.9
Net interest cover (x)	11.0	11.1	10.0	10.9	12.2	13.6

Source: Company data, Deutsche Bank estimates

Investment thesis

Outlook

We now rate HKG as a Sell. We expect the core earnings growth to slow to c.6% in 2015 from a 13% CAGR during 2009-14. It is trading at a 2015E PE of c.25x, much more expensive than Chinese gas utilities peers despite its lower earnings growth profile.

We expect a c.20% yoy decline in the earnings of the new energy business in 2015, after the sharp drop in oil and other commodity prices. HKG had nearly 20% of its total assets invested in this segment as of end-2014, but it generates less than 10% of the company's total earnings. We expect increasing exposure in this business, as the company invests more, to increase HKG's risk profile and lead to a de-rating in HKG's valuation multiples.

We also expect slower earnings growth of 13% in 2015 (from 16% in 2014) for HKG's China gas business. Natural gas is now more expensive than LPG and fuel oil, after two rounds of price hikes in 2013-14 and the sharp drop in oil product prices since Sep 2014. The modest gas price cut of 2.7% (on a blended basis) effective from 1 April 2015 will not help much. The pricing disadvantage, together with a weak macro outlook, is putting pressure on the gas sales volume. In addition, weak new starts in residential property could exert pressure on household connection revenue over the next few years.

Valuation

We value HKG using a sum-of-the-parts (SOTP) approach. Our SOTP target price of HK$15.0 comprises HK$7.0 from the HK gas segment, HK$5.3 from mainland China gas (HK$1.0 of which is from its attributable stake in Towngas China), HK$1.0 from the new energy business, and the rest from property and others. The valuation for its gas businesses in both HK and China is DCF-based, using WACC of 5.7% and 7.9%, respectively.

Risks

The key upside risks include better-than-expected progress and results from the new energy business; higher-than-expected gas sales volume or margins from its mainland gas business; significant value-accretive M&A in city gas projects; and a higher-than-expected increase in the basic tariff for the HK business.

In addition, HKG can do share buybacks, which could help support the share price. The most recent share buybacks occurred on 7-8 October 2014 at an average price of HK$17.0/share.

Derivation of target price

We value HKG using a sum-of-the-parts approach. The bulk (c.47%) of HKG's value, or HK$7.0 per share, is derived from the core HK business, where we assume a WACC of 5.7% (2.7% risk-free rate, 4.9% market risk premium, 0.8x beta, 4% before-tax cost of debt) and growth in our terminal value of 1.0%.

We value HKG’s China gas business at HK$5.3 per share, or 35% of the total value. Of which, HK$1.0 is from HKG’s attributable stake in Towngas China (TCCL, 1083.HK, Hold), based on our target price on TCCL of HK$6.4/share. Aside from Towngas China, we value HKG’s other gas business in China using DCF, assuming a WACC of 7.9% (3.9% risk-free rate, 5.6% market risk premium, 1.0x beta, 5.5% before-tax cost of debt) and terminal growth rate of 2.0%, similar to our assumptions for Chinese gas utilities.

The other businesses are valued using NAV discount (for property, mainly IFC) and a combination of price-to-book multiples and DCF valuation (for the new energy business and other financial investments).

Figure 1: Derivation of target price

Sum of Parts Valuation (end-2015)				
				Comment
Enterprise Value	**(HK$m)**	HK$/share		
Hong Kong gas	76,441			DCF-based assuming WACC of 5.7% and terminal growth of 1%
Mainland utilities (ex. TCCL)	57,497			DCF-based assuming WACC of 7.9% and terminal growth of 2%
HKG's stake in TCCL	10,512			Attributable equity value for HKCG's stake in TCCL (using DB target price for TCCL of HK$6.4/share)
New Energy	19,588			Sum of the parts of major new energy projects, a combination of both DCF valuation and multiples
Property	11,577			Mostly IFC, Based on our property team's NAV estimates and 30% NAV discount
Others	3,683			Incl. available-for-sale and other investments at book value
Total EV	**179,299**			
Less net debt (ex. TCCL)	(14,030)			Excludes net debt of TCCL, as we only include attributable equity value above
Less minority interests (ex. TCCL)	(5,168)			Excludes TCCL, based on 2.0x P/BV
Less perpetuals	(2,354)			
Equity Value	**157,747**	**15.0**	**100%**	Based on 10,512m shares outstanding
HK	74,087	7.0	47%	
China ex TCCL	44,715	4.3	28%	
HKG's stake in TCCL	10,512	1.0	7%	
New Energy	11,000	1.0	7%	
Property	11,577	1.1	7%	
Others	5,855	0.6	4%	

Source: Deutsche Bank estimates

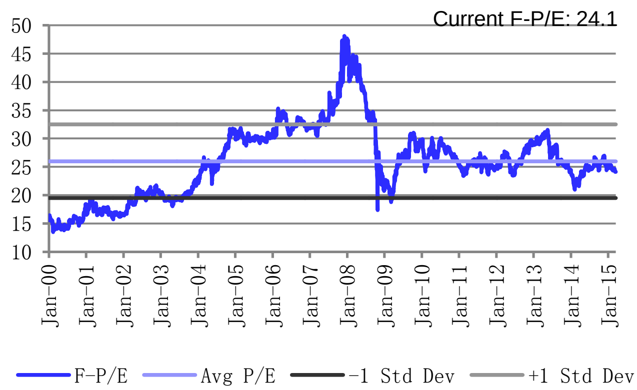
Valuation comparison

HKG used to trade at c.30x PE in 2005-10, except for the period of financial crisis in 2008-09. This was supported by rapid growth from its city gas business in China, where both gas sales volume and attributable segment earnings recorded a c.50% CAGR during 2004-10. The mainland city gas business is still growing, but at a much slower rate (from 25% volume growth in 2010 to c.12% in 2015E). Therefore, although HKG’s forward PE of c.25x does not look high compared to its historical average, we still think the shares are expensive, with core earnings CAGR declining from 13% during 2009-14 to c.6% in 2015E. Its forward P/BV of 3.2x also looks high versus a c.14% ROE.

Investors seem to have given the company the benefit of doubt on its new energy business and pay for its defensiveness. However, we expect criticism on its new energy investment to escalate, due to still disappointing segment earnings after eight years of investment, lack of expertise, and higher risk profile of the upstream projects. The expensive valuation does not leave much room to tolerate earnings misses either, in our view. Our earnings forecasts are 6-8% below consensus for 2015-16. We believe HKG could face a de-rating in

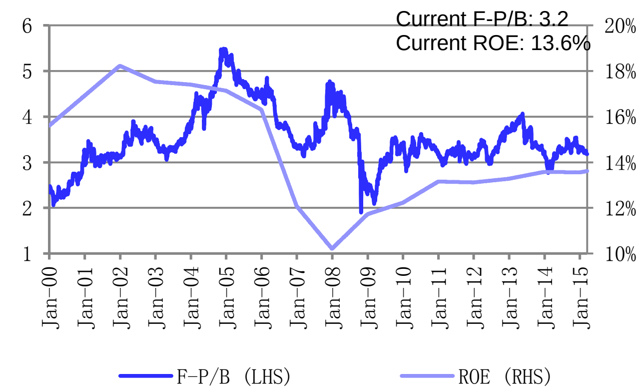
PE multiple when investors become increasingly uncomfortable with the exposure to the new energy business.

Figure 2: HKG 12m forward P/E



Source: Deutsche Bank, Bloomberg Finance LP, Company data

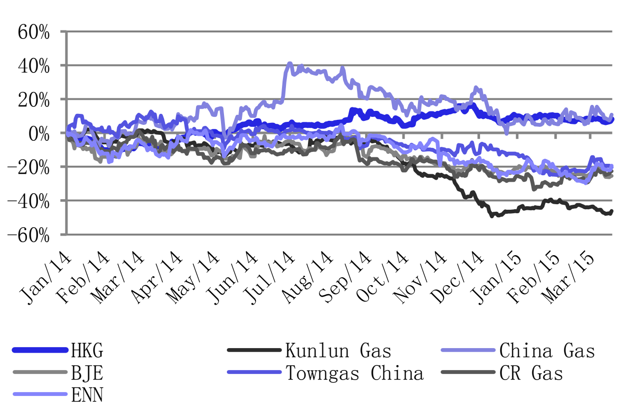
Figure 3: HKG forward P/B vs. ROE



Source: Deutsche Bank, Bloomberg Finance LP, Company data

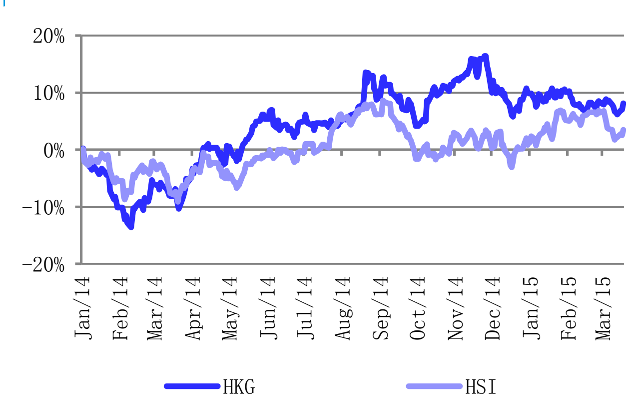
HKG has outperformed Chinese gas utilities by c.30ppt since the beginning of 2014, as the Chinese gas utilities were sold off with market concern on demand weakness and affordability issue of industrial customers after gas price hikes in China. We acknowledge the impact on HKG is smaller, as c.47% of its valuation lies in its Hong Kong gas business, but still, it is difficult to justify such significant outperformance for HKG, with the premium in forward PE multiples expanding to over 50% now (Figure 6). HKG is trading at a 2015E PE of c.25x, higher than Chinese gas utilities peers of 13-22x despite lower earnings growth (7% CAGR in 2014-16E versus 13% on average for peers). HKG is also much more expensive than other HK utilities at 13-16x 2015E PE.

Figure 4:HKG performance vs. China Gas Util. since 2014



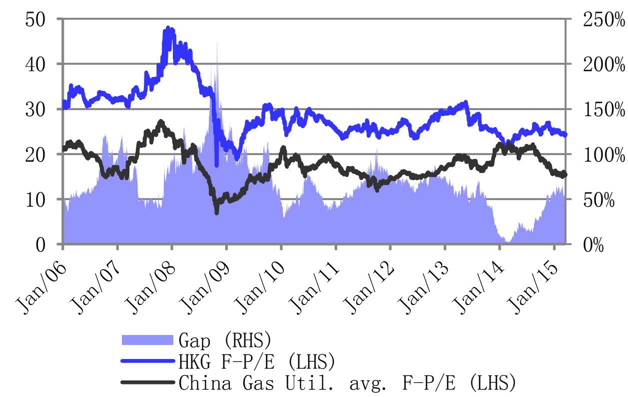
Source: Deutsche Bank, Bloomberg Finance LP

Figure 5: HKG performance vs. Hang Seng Index since 2014



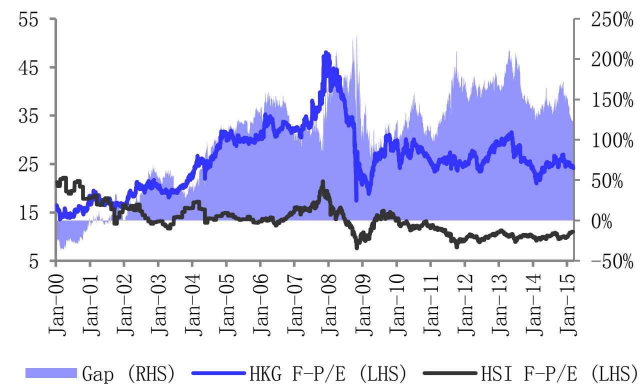
Source: Deutsche Bank, Bloomberg Finance LP

Figure 6: Gap between HKG forward P/E and China Gas Util. forward P/E



Source: Deutsche Bank, Bloomberg Finance LP, Company data

Figure 7: Gap between HKG forward P/E and HSI Index forward P/E



Source: Deutsche Bank, Bloomberg Finance LP, Company data

Figure 8: Valuation comps

Share price as of 3/18/2015								Performance		Valuations											
				Price	% to	Mkt. Cap.	EPS CAGR	Absolute	Relative	P/E		P/BV		Net det/Total capital		RoE		Dividend yield		FCF yield	
Company	Ticker	Price	Rating	target	target	US$m	2014-16E	3m	3m	15E	16E	15E	16E	15E	16E	15E	16E	15E	16E	15E	16E
HK & China Gas	3 HK	HKD17.48	Sell	HKD15.00	(14%)	23,675	7%	2%	(3%)	24.9	22.9	3.3	3.1	19.5	15.8	13.6	13.8	2.2	2.4	2.1	2.5
HK Utilities																					
CLP	2 HK	HKD65.7	Hold	HKD65.00	(1%)	21,379	6%	1%	(4%)	15.6	14.7	1.8	1.7	40.4	40.0	11.9	12.0	4.1	4.2	2.1	3.9
PAH	6 HK	HKD74.85	Hold	HKD77.00	3%	20,575	(2%)	2%	(4%)	19.6	20.6	1.3	1.2	(72.0)	(71.3)	6.5	6.1	3.6	3.6	4.1	3.9
PAH adjusted for cash										13.5	14.2	1.5	1.5			11.2	10.3				
CKI	1038 HK	HKD64.6	Hold	HKD67.00	4%	20,298	(3%)	13%	7%	16.8	17.3	1.5	1.5	8.6	7.8	9.9	8.8	3.3	3.4	0.2	4.1
CKI adjusted for PAH's cash										14.9	15.3	1.7	1.6			11.6	10.7				
				Average				5%	(0%)	16.1x	16.4x	1.6x	1.5x	(7.7)	(7.8)	10.2	9.6	3.6	3.7	2.1	4.0
				Median				2%	(4%)	15.6x	15.3x	1.5x	1.5x	8.6	7.8	11.2	10.3	3.6	3.6	2.1	3.9
China Gas Utilities																					
China Gas	384 HK	HKD7.37	Hold	HKD7.80	6%	7,621	5%	5%	(1%)	13.1	10.3	1.0	1.0	20.2	21.6	8.2	9.7	2.3	2.9	(7.3)	(4.0)
Kunlun Gas	135 HK	HKD12.62	Hold	HKD11.50	(9%)	8,120	15%	5%	(0%)	21.2	19.0	3.3	2.9	38.1	34.3	19.2	18.0	1.3	1.4	0.8	1.1
Beijing Enterprises	392 HK	HKD57.4	Buy	HKD71.40	24%	9,391	23%	(3%)	(8%)	12.9	10.8	1.2	1.1	18.0	16.2	9.5	10.6	2.3	3.2	1.2	3.3
Towngas China	1083 HK	HKD7.17	Hold	HKD6.40	(11%)	2,411	13%	(10%)	(15%)	15.7	14.0	1.3	1.2	24.3	23.2	8.7	9.1	1.4	1.6	(1.8)	(1.4)
CR Gas	1193 HK	HKD20.9	Hold	HKD17.40	(17%)	5,987	10%	8%	2%	17.6	15.7	2.5	2.3	12.3	10.6	15.3	15.2	1.4	1.6	1.3	1.0
ENN Energy	2688 HK	HKD46.2	Hold	HKD39.70	(14%)	6,444	10%	5%	(0%)	17.7	15.6	3.0	2.6	26.8	20.4	19.7	19.1	1.3	1.7	3.6	4.0
				Average				2%	(4%)	16.4x	14.2x	2.1x	1.8x	23.3	21.0	13.4	13.6	1.7	2.1	(0.4)	0.7
				Median				5%	(1%)	16.6x	14.8x	1.9x	1.7x	22.2	21.0	12.4	12.9	1.4	1.7	1.0	1.0

All estimates are DB estimates and all stock data is from Bloomberg Finance LP
*RoE is on a recurring basis

Source: Deutsche Bank, Bloomberg Finance LP, Company data

New energy business – pressure from low oil price

HKG started to invest in new energy business around 2006. According to management, the reason for such a strategic move is that China has a lot of coal reserves but limited oil and gas reserves, and some of the industrial/agricultural waste is not well utilized. Therefore, HKG, through its wholly owned subsidiary EGO, started to engage in developing and applying technologies to convert low-value feedstock to produce crude and natural gas substitutions. Management holds a very optimistic view that this business will deliver high growth in the future.

Figure 9 shows a summary of the projects in the new energy business in mainland China and overseas. HKG has also invested in an aviation fuel storage facility and five LPG stations in Hong Kong, which are classified as new energy business.

In FY14, of the HK$510m in core earnings of the segment, the majority contribution came from the aviation fuel facility in Hong Kong (c.62%), the coal bed methane (CBM) liquefaction project in Shanxi (nearly 20%), and the onshore oil E&P project in Thailand (c.30%), while the coal mines/coal to methanol projects in Inner Mongolia were loss making and the LNG stations were largely break-even as the utilization rate is yet to ramp up, according to management.

Figure 9: Summary of new energy projects in China and overseas

	Location	Stake	Total investment (Rmb m)	Attributable investment (Rmb m)	Capacity	Commissioning date	Notes
Coal mining			**1,997**	**1,038**			
Erdos Xiaoyugou	Inner Mongolia	70.1%	447	313	1.2mtpa, approved to be upgraded to 3mtpa Phase I 0.6mtpa, Phase II	Trial run started in early 2012, commercial operation in 1H13	Delayed from original target of end-2010
Erdos Kejian	Inner Mongolia	100.0%	450	450	1.2mtpa	Acquired in 3Q11	
Fengcheng	Jiangxi	25.0%	1,100	275	0.9mtpa	Trial run in 3Q13	Delayed from original target of 2012
Coal logistic port	**Shandong**	**55.0%**	**540**	**297**	10.6mtpa throughput	Acquired in 2011, started operation in 2Q12	
Coal-based chemical			**2,819**	**1,600**			
Erdos coal to methanol	Inner Mongolia	70.1%	1,170	820	0.2mtpa	Trial run started in 2011, Commercial operation in 4Q13	Delayed from original target of trial run b end-2010, commission by mid-2012
Erdos methanol to gasoline	Inner Mongolia	70.1%	399	280	0.14mtpa	1H15E	
Fengcheng coking plant	Jiangxi	40.0%	1,250	500	1.1mtpa	Operational in two phases in 2013-14	
Oil&gas upstream Projects			**4,275**	**3,234**			
CBM liquefaction	Shanxi	70.0%	600	420	300mn cum pa	Phase I operational in 4Q08, Phase II in Q113	
Tianyuan natural gas field	Jilin	50.0%	140	70	NA	JV established in early 2007	
Songzao CMM liquefaction	Chongqing	50.0%	520	260	91mn cum pa	NA	Delayed from original target of 1Q12
Yangquan CMM liquefaction Project	Shanxi	60.0%	450	270	90mn cum pa	NA	Delayed from original target of 2012
Qianxi CBM E&P	Guizhou	85%	NA	NA	Phase I and II 30mn cum pa each	Exploration started in Nov 2012	Delayed from original commission target of Q214
Daning CBM E&P	Shanxi	NA	NA	NA	140mn cum pa	NA	Delayed from original commission target of Q314
Oilfield	Phetchabun, Thailand	60.0%	US$181m	NA	4,000 barrels of oil per day in 2014	Acquired in July 2012	
Xuzhou coke oven gas to LNG	Jiangsu	80%	488	390	120mn cum pa	3Q15E	
Antai coke oven gas to LNG	Shanxi	60%	633	380	210mn cum pa	2H15E	
Bio Acid Oil to Diesel	Jiangsu	100%	340	340	0.12mtpa	mid-2016E	
CNG/LNG filling statsions in 15 cities	**Shaanxi, Shangdong etc.**	**30%~100%**	**482**	**379**	NA	The first one started in 2006	
9 Telecommunication projects	**Shandong, Liaoning etc.**	**49%~100%**	**890**	**668**	NA	NA	
Other projects	**Jiangsu, Liaoning etc.**	**25%~100%**	**532**	**356**	NA	NA	
Total			**11,535**	**7,573**			

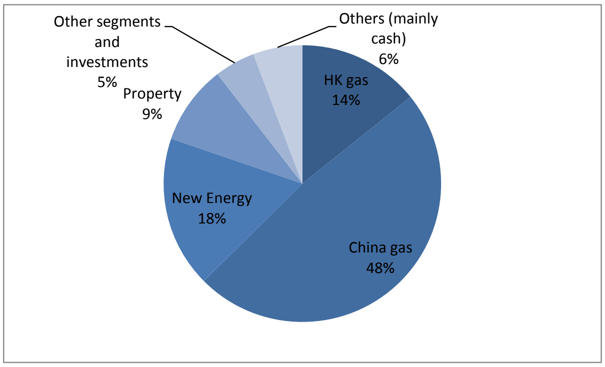
Source: Company data, Deutsche Bank

Earnings contribution still lackluster; lack of transparency remains

Investors seem to have given the company the benefit of doubt in the past several years. However, we are yet to see any meaningful earnings contribution from the new energy segment. In 2014, the new energy business accounted for 18% of the company's total assets, but only c.7% of its total core earnings.

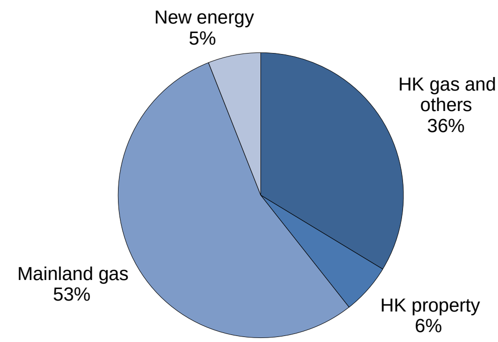
Although the company has improved its disclosure on the new energy business by providing segment information, in our view it is still not transparent enough given the vastly different nature of various projects in the segment.

Figure 10: Total asset mix by segment, end-2014



Source: Company data

Figure 11: Core earnings mix by segment, 2015E

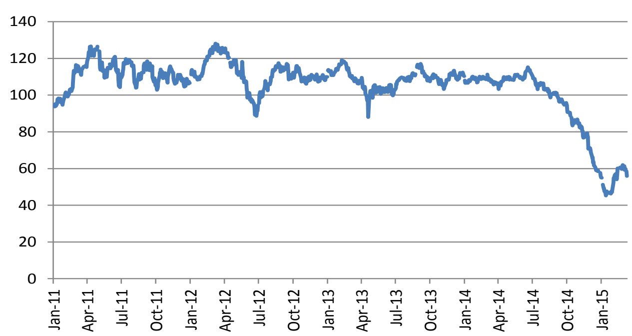


Source: Deutsche Bank estimates

Higher risk profile; lower commodity price dampens return

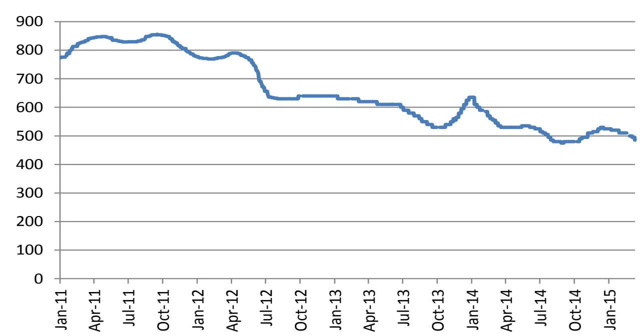
The company management expects over 20% project IRR from the new energy investment in general (higher than over 15% for city gas projects in China). However, there has been a c.40% drop in oil price, c.30% drop in methanol and gasoline price, and c.10% decline in coal price over the past year (Figure 12 to Figure 15). The sharp decline in oil and other commodity prices dampens the returns for some of the projects, such as oil E&P, coal mines, and coal-to-methanol/gasoline projects. In addition, the economic disadvantage of natural gas versus alternative fuels affects demand for LNG, and in turn returns for HKG's LNG refilling stations and CBM liquefaction projects.

Figure 12: Brent oil price (US$/bbl)



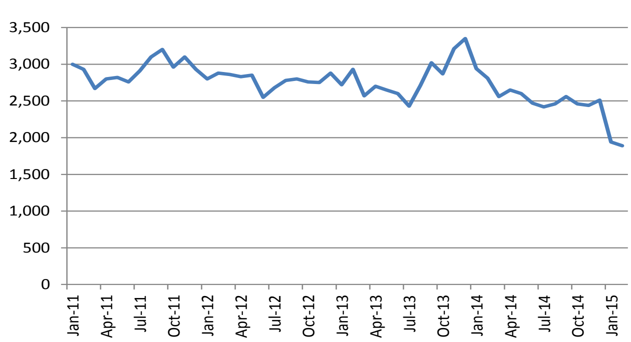
Source: WIND

Figure 13: Qinhuangdao coal price (Rmb/t, incl. VAT)



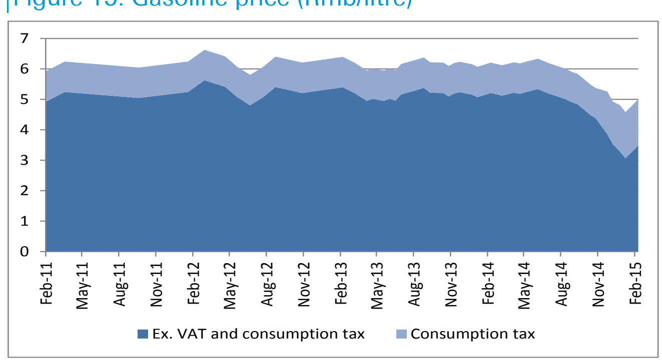
Source: WIND, Deutsche Bank

Figure 14: Methanol price (Rmb/t)



Source: WIND

Figure 15: Gasoline price (Rmb/litre)

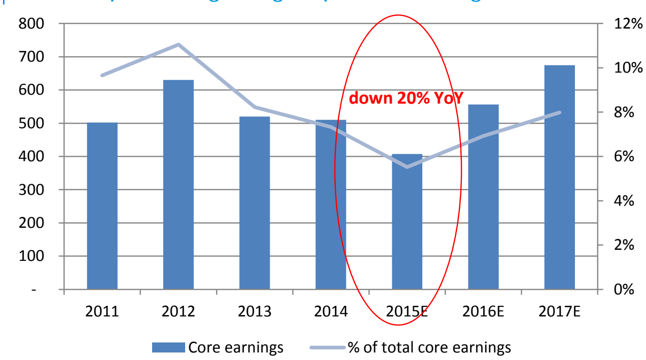


Source: WIND, NDRC, Deutsche Bank

We expect the new energy segment to incur a c.20% yoy earning decline in 2015 before recovering in 2016-17 with a modest recovery in the oil price and new projects coming into operation. But even after the recovery, the earnings contribution from this segment is likely to be less than 10% of the company's total earnings in 2016-17.

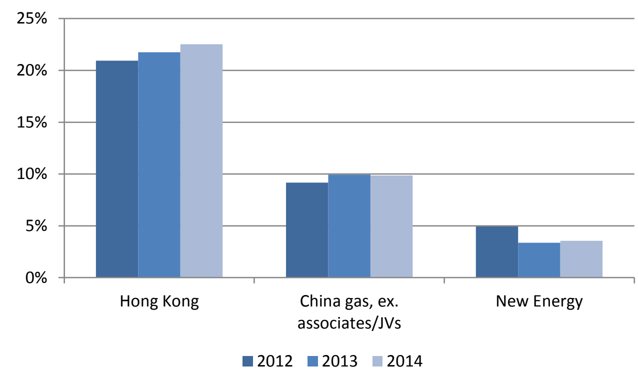
We also see higher implementation risk from the new energy business compared to its city gas business in Hong Kong and mainland China. Coal chemicals and upstream oil and gas E&P involve complex processing and engineering. Although HKG has some experience in this area, it is not its core competency. As shown in Figure 9, there have been delays in the commissioning of several projects.

Figure 16: Core earnings from the new energy business and as a percentage of group core earnings



Source: Company data, Deutsche Bank estimates

Figure 17: Segment EBIT over segment assets



Source: Company data

Mainland China gas – pricing disadvantage vs. alternatives

Natural gas not economically competitive even after 1 April cut

The NDRC has announced the adjustment to the ceiling natural gas price at provincial gate level effective from 1 April 2015. The "incremental volume" tariff will be cut by Rmb0.44/cum and the "base volume" tariff will be raised by Rmb0.04/cum to achieve the pricing converge. Based on the 25/75 incremental/base mix, we estimate that the blended gas price will be modestly reduced by 2.7% at the provincial gate.

To recap on "base volume" and "incremental volume":

- The "base volume" has been set at 112bcm, which is the actual natural gas consumption through pipeline transportation in 2012. The "incremental volume" is any additional volume above the "base volume".
- The provincial gate gas tariff for the "incremental volume" in Shanghai is benchmarked to the market price of fuel oil and LPG, in which the weighting for fuel oil and LPG (on a heat-adjusted basis) would be 60% and 40%, respectively. A 15% discount would then be applied when setting the ceiling natural gas gate tariff. The provincial gate prices for other provinces are referenced to Shanghai gate price considering the transmission distance and affordability.

Figure 18: Blended provincial-gate price change (Shanghai)

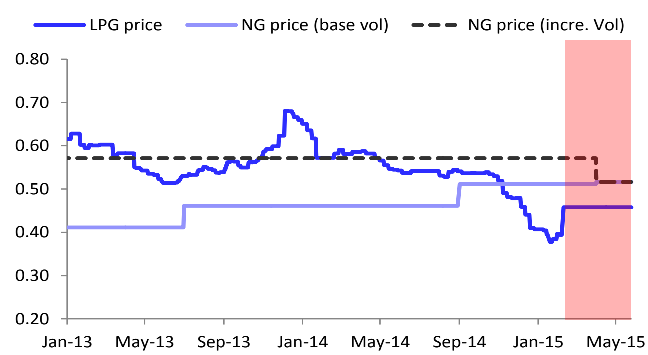
(Rmb/cubic meter)	Sep-14	Volume mix	Chg	Apr-15	Chg (%)
Base	2.84	75%	0.04	2.88	1.4%
Incremental	3.32	25%	-0.44	2.88	-13.3%
Average	**2.94**			**2.88**	**-2.7%**

Source: NDRC, Deutsche Bank estimates

However, even after the price cut, we estimate the price competitiveness of natural gas versus alternative fuels to remain unfavorable after the sharp oil price decline over the past 12 months – the price of converged natural gas versus LPG and diesel will likely remain at a 1-13% premium (versus a 20% discount in February 2014), while the premium to fuel oil has been widened to 67% (from 7% in February 2014).

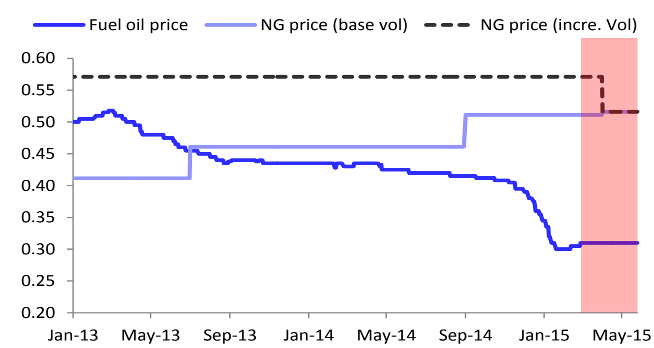
Combined with a still-weak macro outlook, we see risks of volume growth or compromised margins of gas distributors, especially for sales to certain industrial and vehicle users. For more details, please see *China Gas Utilities – Small cut in blended gas price won't help, maintaining Hold*, published on 2 March 2015.

Figure 19: Natural gas price vs. LPG price



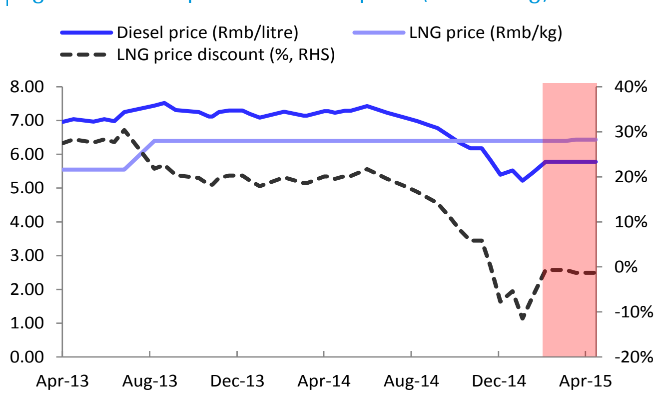
Source: Deutsche Bank, WIND

Figure 20: Natural gas price vs. fuel oil price



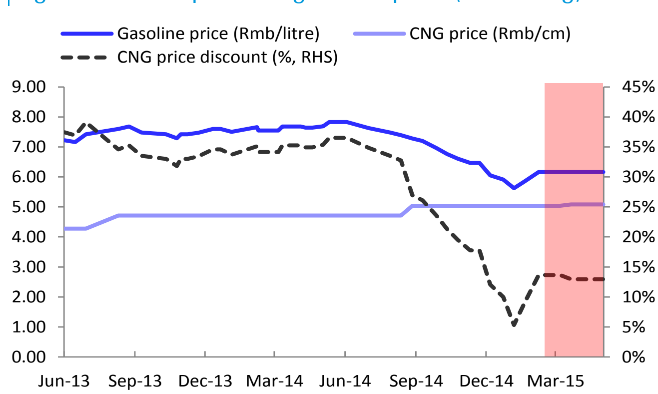
Source: Deutsche Bank, WIND

Figure 21: LNG price vs. diesel price (Shandong)



Source: Deutsche Bank, WIND

Figure 22: CNG price vs. gasoline price (Shandong)



Source: Deutsche Bank, WIND

Will the natural gas price be cut in 2H15?

There is a view in the market that after the NDRC converges the natural gas price from 1 April 2015, there will be a further cut to the unified price in 2H15. However, the NDRC did not specify in its announcement any future price adjustments for non-direct supply users (timing, pricing formula, etc), and we believe it is still premature to assume another tariff cut in 2H15.

- We understand that the NDRC's goal is to reform natural gas pricing to be market-oriented. The Shanghai Natural Gas Trading Center will be established this year to create China's own Henry Hub price. The "net-back" pricing mechanism is actually not a market-oriented pricing mechanism. The real market price should be concluded on negotiation between buyers and sellers, considering the demand/supply dynamics of natural gas, rather than the prices of substitute fuels. In this regard, NDRC may not be keen to adjust the price again, after the three-step pricing reform is completed.
- Even though the NDRC still sets the price, the 15% discount rate used in the "net-back" pricing formula could be revised. Such a discount was used to prevent natural gas prices from rising too quickly when the oil price was over US$100/bbl in 2013. With the oil price having fallen dramatically, the discount may be narrowed or removed.
- The NDRC may hold back from cutting provincial gate gas prices to encourage investment in domestic production, especially in unconventional gas. Moreover, PetroChina will likely object to further cuts to avoid widening losses again, as the imported prices of some pipe gas or LNG are not fully linked to the oil price.
- The NDRC may selectively cut the gas price for some users, such as power plants. However, city gas distributors will not benefit, as most power plants are directly supplied by the three upstream gas suppliers.

Connection revenue could face risk

New starts in residential property GFA declined by 14% yoy in 2014, which is likely to exert pressure on residential connection fees with a 6-12-month lag. Demand weakness in commercial/industrial users makes residential growth more critical, especially from old houses with a lower margin. We suspect the high-margin connection business, which still accounts for c.20% of HKG's earnings, could face revenue downside in the medium term.

Hong Kong Gas – potential tariff hike factored in

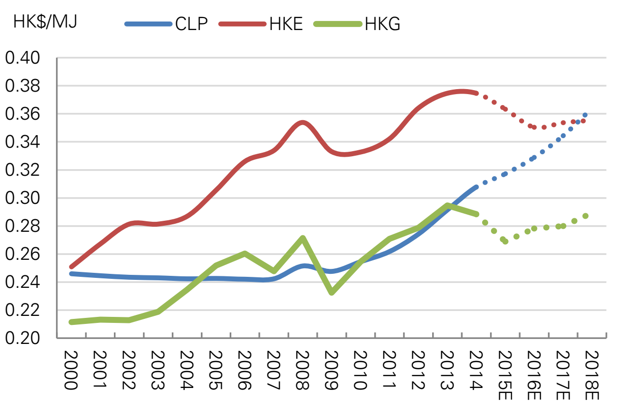
HKG's gas business in Hong Kong is not regulated. In theory, HKG is free to raise its basic tariff (only needs to give three months' notice to the HK government), but it needs to keep its tariffs competitive against electricity. Currently, we estimate HKG's gas tariff is c.15% cheaper than CLP's electricity tariff and c.26% cheaper than HKE's electricity tariff on a heat-adjusted basis.

We note that CLP's tariff is likely to rise in the next few years, due to the increasing usage of natural gas to meet the emission cap and rising fuel cost from more expensive natural gas from Central Asia. This will increase the pricing gap between gas and power on a heat-adjusted basis, suggesting some scope for the HK gas tariff to piggy-back without losing its competitiveness (Figure 23 and Figure 24).

About 50% of HKG's fuel cost is fixed at low levels under the long-term LNG supply contract from Australia. The decline in oil price and naptha cost also works in HKG's favor, as it can help reduce the fuel cost surcharge and leaves larger upside potential in the non-fuel portion of the tariff (i.e. basic tariff), although HKG will likely be very careful about the pace and the amount of raising basic tariff to avoid the risk of inviting political pressure to regulate its return.

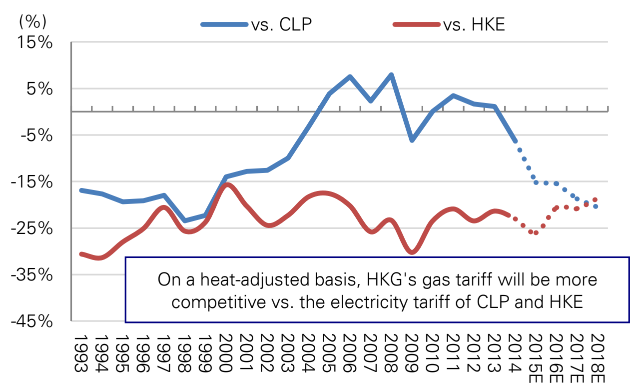
HKG has pledged to the HK government that it will not raise the basic gas tariff in Hong Kong before April 2015. Considering the three months' notice period to the HK government, we believe that HKG could raise basic tariff again later this year. We have factored in a HK$0.01/MJ tariff hike, or 4.4%, effective from 1 October 2015. The company recently raised basic tariff by HK$0.003/MJ in 1 October 2008, by HK$0.006/MJ in 1 April 2010, and by HK$0.01/MJ in 1 April 2013.

Figure 23: HK gas tariff and CLP/PAH's electricity tariffs



Source: Deutsche Bank estimates, Company data

Figure 24: HK gas tariff vs. CLP/PAH's electricity tariffs



Source: Deutsche Bank estimates, Company data

Earnings review and forecasts

FY14 results review

HKG announced its FY14 results on 18 March after market close. Reported net profit was up 4% yoy to HK$7.1bn, mainly due to a 13% yoy increase in gas sales volume in Mainland China. Stripping out one-offs such as property revaluation gain and FX gain/loss, recurring earnings were up 10% yoy to HK$7.0bn. This was c.2% below our estimate and c.5% below consensus, mainly on weak result from the new energy business with segment earnings down 2% yoy.

Dividend per share was HK$0.35, up 10% yoy after adjusting for the bonus share issuance, in line with our estimate.

Key assumptions and earnings sensitivity

We expect HKG's earnings growth to slow from 13% in 2009-14 to 6% in 2015 and 7% CAGR in 2014-17, due to challenges for its new energy business on lower oil/commodity prices, and slower growth in its gas business in China as natural gas is economically uncompetitive in a weak macro environment.

Figure 25: Core earnings breakdown by segment

(HK$ m)	2012	2013	2014	2015E	2016E	2017E
HK gas and others	2,091	2,386	2,522	2,639	2,748	2,789
HK property	428	454	498	455	413	406
Mainland gas	2,551	2,960	3,430	3,877	4,320	4,580
New energy	630	520	510	407	556	675
Total core earnings	**5,700**	**6,320**	**6,960**	**7,378**	**8,037**	**8,450**
Earnings mix						
HK gas	37%	38%	36%	36%	34%	33%
HK property	8%	7%	7%	6%	5%	5%
Mainland gas	45%	47%	49%	53%	54%	54%
New energy	11%	8%	7%	6%	7%	8%
Total	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**
Earnings growth						
HK gas		14%	6%	5%	4%	2%
HK property		6%	10%	-9%	-9%	-2%
Mainland gas		16%	16%	13%	11%	6%
New energy		-17%	-2%	-20%	36%	21%
Total		**11%**	**10%**	**6%**	**9%**	**5%**

Source: Company data, Deutsche Bank estimates

Figure 26 shows our key assumptions for HKG's gas business in Hong Kong and China:

For Hong Kong gas business, we assume gas volume growth of c.1% pa and basic tariff hike of HK$0.01/MJ, or 4.4%, effective 1 October 2015, before another hike in April 2018.

For mainland China gas business:

- Gas sale volume was up 14% yoy to 15.2bcm in 2014. We assume 17bcm of gas sales volume in 2015 (up 12% yoy), in line with management guidance. Management still guides for double-digit growth in gas sales volume for next five years.
- We have allowed for the temporary margin compression from the 1 Sep 2014 gas cost hike to be restored in 2015, and the gross margin for C&I sales to remain stable at c.Rmb0.86/cum going forward versus Rmb0.25/cum for residential gas sales. For every Rmb0.01/cum lower gross margin, there would be 1.1% downside to our earnings estimates (Figure 27).
- We still assume modest connection revenue growth of 10% in 2015, with penetration rate at c.50%. But we acknowledge that a slowdown or eventual decline would be a longer-term concern.

  We have allowed for stable connection gross margin of 70% in 2015-16E, before trending down to 68% in 2017E and 65% in 2018E.

Figure 26: Key assumptions for the Hong Kong and China gas businesses

	2012	2013	2014	2015E	2016E	2017E
HK gas business:						
Basic tariff (HK$/MJ)	**0.219**	**0.229**	**0.229**	**0.239**	**0.239**	**0.239**
Basic tariff hike (HK$/MJ)	-	0.010	-	0.010	-	-
Weightings		0.750		0.250		
Avg. basic tariff (HK$/MJ)	**0.219**	**0.226**	**0.229**	**0.231**	**0.239**	**0.239**
yoy	0%	3%	1%	1%	3%	0%
Gas sales vol. (TJ)	28,360	28,556	28,835	29,182	29,534	29,829
yoy	1%	1%	1%	1%	1%	1%
Mainland gas business:						
Total gas sales volume (mn cum), all entities	**11,900**	**13,400**	**15,200**	**17,022**	**18,778**	**20,299**
YoY	16%	13%	13%	12%	10%	8%
% of residential	24%	23%	24%	23%	23%	23%
Total gas sales volume (mn cum), consolidated, ex. TCCL	**1,612**	**1,825**	**2,058**	**2,306**	**2,557**	**2,774**
Residential (mn cum)	376	405	491	518	574	631
C&I (mn cum)	1,236	1,420	1,567	1,788	1,983	2,143
Average gas tariff (Rmb/cum), ex. TCCL	**3.39**	**3.42**	**3.57**	**3.86**	**3.86**	**3.85**
Residential	2.41	2.41	2.41	2.41	2.41	2.41
C&I	3.69	3.71	3.94	4.28	4.28	4.28
Average cost of gas purchases (Rmb/cum), ex. TCCL	**2.59**	**2.67**	**2.88**	**3.14**	**3.14**	**3.13**
Residential	2.16	2.16	2.16	2.16	2.16	2.16
C&I	2.72	2.82	3.11	3.42	3.42	3.42
Gap between gas tariff (Rmb/cum), ex. TCCL	**0.80**	**0.75**	**0.69**	**0.72**	**0.72**	**0.72**
Residential	0.25	0.25	0.25	0.25	0.25	0.25
C&I	0.97	0.89	0.83	0.86	0.86	0.86
Gap between gas tariff (Rmb/cum), incl. TCCL	**0.69**	**0.67**	**0.64**	**0.67**	**0.67**	**0.67**
Connected Households (mn), all entities	7.20	8.80	9.80	10.90	12.03	13.17
Additions (mn)	0.67	1.60	1.00	1.10	1.13	1.13
yoy	6%	139%	-38%	10%	3%	0%
Penetration rate	48%	50%	52%	55%	58%	61%
Average connection fee (Rmb/household), ex. TCCL	**3,500**	**3,500**	**3,500**	**3,500**	**3,500**	**3,325**
yoy		0%	0%	0%	0%	-5%
Average connection cost (Rmb/household), ex. TCCL	(1,050)	(1,050)	(1,050)	(1,050)	(1,050)	(1,050)
Gross margin, ex. TCCL	**70%**	**70%**	**70%**	**70%**	**70%**	**68%**

Note: The sharp increase of connected households in 2013 was due to the acquisition of Hangzhou project.
Source: Company data, Deutsche Bank estimates

Figure 27: Earnings sensitivity

	2015E	2016E	2017E
1% higher HK gas sales volume	0.6%	0.5%	0.5%
1% higher HK gas selling prices	0.7%	0.7%	0.7%
1% lower gas sales volume in China	-0.8%	-0.8%	-0.9%
Rmb0.01/cum lower gross margin on gas sales in China	-1.1%	-1.1%	-1.2%
1ppt lower connection margin	-0.4%	-0.4%	-0.4%

Source: Deutsche Bank

For the new energy segment, we expect the earnings to drop c.20% yoy in 2015 and account for only c.6% of HKG's total core earnings, before recovering in 2016-17 with a modest recovery in oil price and with new projects commissioned and ramped up. Management expects good return from the methanol-to-gasoline project (trial run started in 4Q14), two coke-oven gas to LNG projects (to start operation late this year) and palm oil residue to diesel (to start operation in mid 2016).

We assume Brent oil price of US$59/bbl (-40% yoy) in 2015, US$70/bbl (+18% yoy) in 2016 and US$75/bbl (+7% yoy) in 2017, in line with our oil research team's forecasts. This is partially offset by an increase in Thai oil production volume from less than 4,000bbl/d in 2014 to 6,000bbl/d in 2015E. We assume 15-25% ROI for projects under construction. We estimate every US$5/bbl lower oil price could reduce HKG's earnings by c.1%.

We have not factored in any new energy projects that have not yet been announced by management. However, company management indicated at the analyst briefing that a total of c. HK$15bn in capex is planned in the coming three years and the majority will be allocated to the new energy business. We think this could further add to earnings volatility.

Figure 28: Earnings forecasts for new energy segment

(HK$ m)	2011	2012	2013	2014	2015E	2016E	2017E
Hong Kong:	**259**	**255**	**285**	**318**	**305**	**305**	**305**
Aviation fuel facility	233	233	258	275	275	275	275
LPG business	26	22	27	43	30	30	30
Mainland China:	**243**	**323**	**180**	**42**	**20**	**150**	**233**
CBM liquefaction	31	38	44	85	118	124	132
Coal-to-methanol project	8	94	68	30	(47)	(23)	(11)
Coal mine + logistics	203	190	67	(73)	(87)	(95)	(78)
LNG stations	-	-	-	-	5	20	30
Coke oven gas to LNG	-	-	-	-	9	36	72
Methanol to gasoline	-	-	-	-	22	88	88
Overseas:	**-**	**52**	**55**	**150**	**83**	**101**	**137**
Thailand oil E&P	-	52	55	150	83	101	137
Total core earnings	**502**	**630**	**520**	**510**	**407**	**556**	**675**
YoY		25%	-17%	-2%	-20%	36%	21%
% of company total	**10%**	**11%**	**8%**	**7%**	**6%**	**7%**	**8%**

Note: The company only disclosed the total core earnings from the new energy segment. The breakdown by major projects is our estimates.
Source: Company data, Deutsche Bank estimates

Deutsche Bank versus consensus

Our reported earnings forecasts are 12% below consensus in 2015-16, while our core earnings forecasts are 6-8% below consensus. We believe this is partly because we do not factor in any property revaluation in our core earnings forecast. We also believe the consensus may have not updated for the negative earnings impact from lower oil prices on HKG's new energy business.

Figure 29: Deutsche Bank vs. consensus

	Reported net profits		Recurring net profits		Recurring EPS (HK$)		DPS (HK$)	
HK$ m	**2015E**	**2016E**	**2015E**	**2016E**	**2015E**	**2016E**	**2015E**	**2016E**
DB	7,378	8,037	7,378	8,037	0.70	0.76	0.39	0.42
Consensus	8,374	9,087	7,865	8,771	0.76	0.83	0.38	0.40
Diff vs. consensus	-12%	-12%	-6%	-8%	-7%	-8%	2%	6%

Source: Deutsche Bank, Bloomberg Finance LP

Figure 30: Income statements

Consolidated P&L	2012	2013	2014	2015E	2016E	2017E
(HK$ mil., except noted otherwise)						
Revenue	**24,923**	**28,246**	**31,615**	**34,133**	**37,016**	**39,758**
yoy	*11%*	*13%*	*12%*	*8%*	*8%*	*7%*
HK utilities and headquarter	9,117	9,620	9,600	9,175	9,588	9,759
Mainland utilities (excl. TCCL)	7,904	9,445	10,968	13,060	14,354	15,371
Towngas China (TCCL)	5,183	6,716	7,882	9,205	10,265	11,458
New Energy	2,680	2,423	3,112	2,644	2,758	3,116
Property	38	42	52	49	51	54
Others	(0)	0	(0)	0	0	0
Operating expense	(17,369)	(19,897)	(22,402)	(24,648)	(26,826)	(29,121)
yoy	*12%*	*15%*	*13%*	*10%*	*9%*	*9%*
HK utilities and headquarter	(5,633)	(6,017)	(5,809)	(5,207)	(5,340)	(5,369)
Mainland utilities (excl. TCCL)	(5,913)	(6,908)	(8,025)	(10,020)	(11,052)	(11,932)
Towngas China (TCCL)	(4,164)	(5,460)	(6,595)	(7,853)	(8,797)	(9,938)
New Energy	(1,704)	(1,567)	(2,051)	(1,647)	(1,715)	(1,960)
Property	(17)	(20)	(24)	(23)	(24)	(25)
Others	62	75	102	102	102	102
EBITDA	**7,553**	**8,349**	**9,213**	**9,485**	**10,191**	**10,637**
EBITDA margin	*30%*	*30%*	*29%*	*28%*	*28%*	*27%*
HK utilities and headquarter	3,484	3,603	3,792	3,968	4,248	4,390
Mainland utilities (excl. TCCL)	1,991	2,537	2,943	3,041	3,303	3,440
Towngas China (TCCL)	1,019	1,256	1,286	1,352	1,468	1,520
New Energy	976	856	1,061	997	1,043	1,156
Property	21	22	28	26	28	29
Others	62	75	102	102	102	102
Deprec. and amort	(1,465)	(1,649)	(1,952)	(2,207)	(2,255)	(2,339)
EBIT	**6,088**	**6,700**	**7,261**	**7,279**	**7,936**	**8,298**
EBIT margin	*24%*	*24%*	*23%*	*21%*	*21%*	*21%*
HK utilities and headquarter	2,867	2,963	3,134	3,291	3,557	3,686
Mainland utilities (excl. TCCL)	1,598	2,050	2,391	2,404	2,632	2,738
Towngas China (TCCL)	756	954	905	936	1,006	1,034
New Energy	795	646	716	536	627	725
Property	21	22	28	26	28	29
Others	52	64	86	86	86	86
Net interest income/(expense)	(551)	(599)	(726)	(663)	(650)	(608)
Other income	245	611	157	357	357	357
Share of profit from JCE & assoc.	3,655	2,672	3,215	3,202	3,432	3,623
Exceptionals	449	27	(32)	0	0	0
Profit before tax	**9,886**	**9,411**	**9,875**	**10,175**	**11,076**	**11,670**
Taxation	(1,485)	(1,655)	(1,771)	(1,796)	(1,964)	(2,077)
effective tax rate (%)	*24%*	*25%*	*27%*	*26%*	*26%*	*26%*
Profit after tax	**8,401**	**7,756**	**8,103**	**8,378**	**9,112**	**9,594**
Minority interest	(689)	(902)	(892)	(889)	(964)	(1,032)
Perpetuals	0	0	(102)	(112)	(112)	(112)
Net profit	**7,712**	**6,854**	**7,109**	**7,378**	**8,037**	**8,450**
net margin	*31%*	*24%*	*22%*	*22%*	*22%*	*21%*
yoy	*25%*	*-11%*	*4%*	*4%*	*9%*	*5%*
Core earnings	**5,700**	**6,320**	**6,960**	**7,378**	**8,037**	**8,450**
yoy	10%	11%	10%	6%	9%	5%
HK	2,519	2,840	3,020	3,094	3,161	3,195
yoy	-4%	13%	6%	2%	2%	1%
China	2,551	2,960	3,430	3,877	4,320	4,580
yoy	22%	16%	16%	13%	11%	6%
New Energy	630	520	510	407	556	675
yoy	25%	-17%	-2%	-20%	36%	21%
Per share						
Weighted avg. shares - diluted (mm)	10,516	10,516	10,515	10,512	10,512	10,512
Diluted EPS (HK$)	0.73	0.65	0.68	0.70	0.76	0.80
Diluted recurring EPS (HK$)	0.54	0.60	0.66	0.70	0.76	0.80
Recurring EPS growth	*10%*	*11%*	*10%*	*6%*	*9%*	*5%*
DPS (HK$)	0.29	0.32	0.35	0.39	0.42	0.47
Dividend payout ratio	*53%*	*53%*	*53%*	*55%*	*55%*	*58%*

Source: Company data, Deutsche Bank estimates

Figure 31: Balance sheet and cash flow statements

Consolidated balance sheet	2012	2013	2014	2015E	2016E	2017E
(HK$ mil., except noted otherwise)						
Long Term Assets	**77,980**	**85,842**	**90,441**	**93,144**	**95,525**	**97,197**
Net PP&E	41,914	47,002	51,354	52,880	53,990	54,339
Goodwill and intangibles	3,845	5,253	5,859	5,859	5,859	5,859
Interest in JCE and assoc.	26,345	27,735	27,961	29,138	30,408	31,731
Other investments	5,876	5,851	5,268	5,268	5,268	5,268
Others	0	0	0	0	0	0
Current Assets	**21,044**	**20,554**	**23,970**	**26,990**	**30,546**	**34,845**
Cash and liquid assets	12,186	8,849	12,606	14,826	17,623	21,206
Inventory	1,832	2,383	2,283	2,753	2,992	3,235
Receivables	5,722	6,568	6,976	7,306	7,826	8,298
Customer deposits	261	1,289	550	550	550	550
Others	1,042	1,465	1,556	1,556	1,556	1,556
Current Liabilities	**17,253**	**19,262**	**20,690**	**21,760**	**22,677**	**23,560**
Short-term debt	6,491	6,222	7,050	7,050	7,050	7,050
Tax payable	878	829	896	806	817	893
Account payable	7,945	9,284	11,227	11,897	12,956	13,796
Others	1,939	2,927	1,517	2,008	1,854	1,821
Long Term Liabilities	**31,304**	**30,763**	**31,498**	**31,778**	**32,084**	**32,405**
Long-term debt	25,230	24,401	24,484	24,484	24,484	24,484
Others	6,074	6,362	7,013	7,294	7,599	7,921
Minority Interest	**5,148**	**6,503**	**7,242**	**8,042**	**8,907**	**9,828**
Perpetuals	**-**	**-**	**2,354**	**2,354**	**2,354**	**2,354**
Shareholders Funds	**45,319**	**49,868**	**52,628**	**56,200**	**60,050**	**63,895**

Balance Sheet Ratios						
BVPS (end of period balance)	4.31	4.74	5.01	5.35	5.71	6.08
Total debt	33,998	33,190	34,315	34,341	34,366	34,392
Net debt (cash)	21,550	23,052	21,160	18,965	16,193	12,636
Net debt / equity	43%	41%	34%	28%	23%	17%
Net debt / equity (excl. minority interest)	48%	46%	40%	34%	27%	20%

Consolidated cashflow statement	2012	2013	2014E	2015E	2016E	2017E
EBITDA	**7,553**	**8,349**	**9,213**	**9,485**	**10,191**	**10,637**
Adjustments	436	(56)	362	260	81	117
Tax paid	(1,323)	(1,301)	(1,404)	(1,529)	(1,608)	(1,730)
Cashflow from operations	**6,666**	**6,992**	**8,170**	**8,216**	**8,663**	**9,024**
Investing cashflow	**(6,615)**	**(6,059)**	**(3,436)**	**(1,175)**	**(670)**	**146**
Capex (excl. cap. interest)	(5,906)	(5,294)	(6,127)	(3,557)	(3,190)	(2,511)
Purchase of investments / securities	(2,047)	(2,142)	0	0	0	0
Dividends received	1,494	1,815	2,179	2,357	2,495	2,632
Disposal	436	(312)	583	0	0	0
Others	(592)	(127)	(71)	25	25	25
Financing cashflow	**892**	**(4,350)**	**(2,167)**	**(4,820)**	**(5,197)**	**(5,587)**
Net proceeds from share issuance	0	0	0	0	0	0
Net proceeds from borrowing	6,234	(1,050)	0	0	0	0
Dividends paid	(4,243)	(3,146)	(3,461)	(3,806)	(4,186)	(4,605)
Net interest (paid) / received	(789)	(881)	(902)	(839)	(826)	(784)
Others (incl. contribution from minority)	(310)	726	2,196	(175)	(184)	(197)
FX adj. and others	(2)	(79)	(1,189)	0	0	0
Net cashflow	**941**	**(3,496)**	**1,379**	**2,220**	**2,797**	**3,583**

Note: The 2014 cash flow numbers are our estimates pending actual disclosure from annual report
Source: Company data, Deutsche Bank estimates

Appendix 1

Important Disclosures

Additional information available upon request

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Company	Ticker	Recent price*	Disclosure
Hong Kong & China Gas	0003.HK	17.54 (HKD) 18 Mar 15	NA

*Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg and other vendors . Data is sourced from Deutsche Bank and subject companies.

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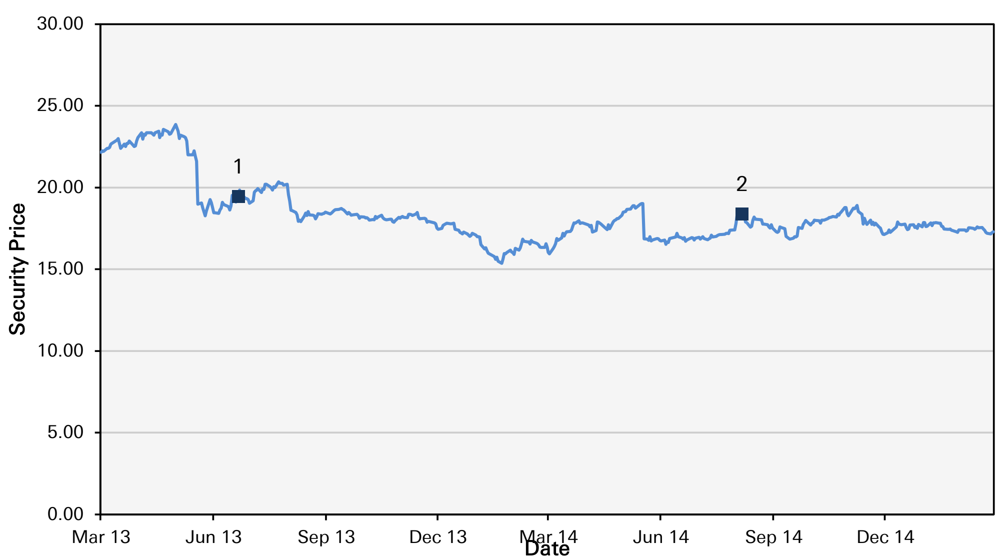
Historical recommendations and target price: Hong Kong & China Gas (0003.HK)
(as of 3/18/2015)



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Strong Buy
Buy
Market Perform
Underperform
Not Rated
Suspended Rating

Current Recommendations

Buy
Hold
Sell
Not Rated
Suspended Rating

*New Recommendation Structure as of September 9,2002

1. 10/07/2013: Hold, Target Price Change HKD17.60
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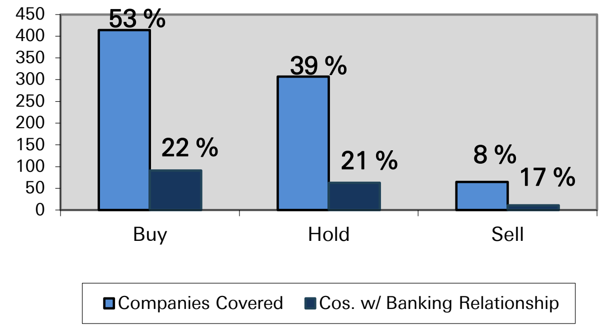

Asia-Pacific Universe

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