

JPM-pp1

Asia Pacific Equity Research

19 March 2015

Datang International - H (991 HK)

Neutral

Price: HK\$3.76

18 Mar 2015

Price Target: HK\$4.10

PT End Date: 31 Dec 2015

Strong FY14 profit growth from power business offset by losses on coal chemical / coal mine businesses

- **Power business the key focus in 2014:** Datang announced their FY14 results overnight. As the company has already announced the plan to dispose of its coal-to-chemical business last July, the key focus turned to its power business. In this respect, the company's power business delivered a +25% Y/Y profit growth. The strong profit growth was mainly driven by falling coal prices (fuel costs down 10.5% Y/Y). That said, the strong profit growth was largely offset by: (1) widening losses from the coal chemical business (Rmb 3.4B LBT in 2014 (before impairment provisions, vs. Rmb 2.2B losses in 1H2013) and (2) a pre-tax loss of 100MM in the coal mine business (before provision).
- **Coal-to-chemical business** suffered an Rmb3.4Bn pre-tax loss (before provision) in chemical segment. (2013: Rmb 2.2B and 1H2014: Rmb 1.4B) mainly due to lower revenue (down 27% Y/Y) and increase in depreciation (up by Rmb670MM).
- **Ningde turnaround:** After the overhaul in 1H2014, Ningde nuclear power plant enjoyed a significant turnaround in 2H2014 with a > Rmb 700MM profit (+ >170% Y/Y) vs. Rmb 116MM loss in 1H2014. #3 and #4 are expected to start commercial operation in Mid-15 and Aug-16, respectively.
- **Unit fuel cost decreased by 10.5% Y/Y** to Rmb145/MWh in 2014 (vs.-11% Y/Y in 1H14) due to falling coal prices. In particular, 2H14 unit fuel costs declined to Rmb 140 / MWh (down 10% Y/Y and 10% H/H).
- **FCF turned positive** to ~Rmb 3.3B in 2014 (2013: -ve Rmb 5Bln).
- **Impairment provision:** Consistent with an announcement made earlier this year, the company made a Rmb3.3B impairment provisions (Rmb1.3B in 2013), comprising 1.5Bn on assets of coal-mine business, 1.8Bn on assets of chemical business. We believe this was part of management's plan to dispose of its coal-chemical business.
- **Net gearing** slightly increased to 391% as of Dec 2014 from 383%/385% in Jun-14/Dec-13.
- **Coal-chemical disposal the key catalyst:** Share price has underperformed the market by >10% YTD amidst market fears of potential tariff cut in the NT, and a lack of concrete development in the coal-chemical disposal. On a relative basis, CPI is our top pick in the IPP spaces thanks to its significant exposure to hydropower (no tariff cut risks) and inland coal-fired plants (less utilization downside).
- **Analyst briefing** will be held on 20 March 2015 (Friday) at 9:30AM. Location: Ballroom C, Level 5, Island Shangri-La Hong Kong, Two Pacific Place, Supreme Court Road, Central, Hong Kong.

Table 1: Summary of 2014 results under IFRS (In RMB MM unless otherwise specify)

(in RMB MM)	1H12	1H13	1H14	2H12	2H13	2H14	Y/Y	2012	2013	2014	Y/Y
Revenue	36,877	37,010	34,843	40,721	38,217	35,352	(7)	77,598	75,227	70,194	(7)
Power generation segment	33,395	32,198	31,232	35,097	33,431	33,175	(1)	68,492	65,629	64,406	(2)

Coal segment	1,779	2,437	1,451	4,204	1,773	317	(82)	5,983	4,210	1,768	(58)
Chemical segment	1,420	1,790	1,409	1,160	3,147	2,210	(30)	2,580	4,938	3,619	(27)
Other segments	283	584	750	260	(134)	(350)	162	544	450	400	(11)
Fuel cost from power generation	(20,382)	(15,774)	(13,728)	(18,734)	(15,368)	(13,710)	(11)	(39,116)	(31,142)	(27,438)	(12)
Fuel cost from coal sales	(1,533)	(2,367)	(1,396)	(3,820)	(1,570)	(339)	(78)	(5,353)	(3,937)	(1,735)	(56)
Repairs and maintenance	(921)	(1,026)	(997)	(1,441)	(1,385)	(1,328)	(4)	(2,362)	(2,411)	(2,325)	(4)
Salaries and staff welfare	(1,051)	(1,593)	(1,278)	(1,697)	(1,227)	(1,979)	61	(2,748)	(2,820)	(3,257)	15
Others	(2,760)	(4,096)	(4,110)	(2,931)	(5,485)	(6,830)	25	(5,691)	(9,581)	(10,939)	14
EBITDA	10,230	12,154	13,335	12,098	13,183	11,166	(15)	22,329	25,337	24,500	(3)
Depreciation	(4,369)	(4,882)	(5,278)	(4,492)	(5,133)	(6,173)	20	(8,861)	(10,015)	(11,451)	14
EBIT	5,862	7,272	8,057	7,606	8,050	4,992	(38)	13,468	15,322	13,049	(15)
Associates & JCE	471	578	184	322	243	535	120	792	821	719	(12)
Interest Income	40.35	39.958	41.855	31.518	39.546	47	19	72	80	89	12
Investment Income	266	223	86	208	127	134	6	474	350	220	(37)
Interest expense	(4,272)	(4,083)	(4,233)	(4,296)	(4,272)	(4,471)	5	(8,568)	(8,356)	(8,704)	4
Others (including gains/loss, impairment)	1	(17)	-	1,304	(242)	(201)	(17)	1,306	(258)	(201)	(22)
Profit before tax	2,368	4,013	4,136	5,176	3,945	1,036	(74)	7,544	7,959	5,172	(35)
Power generation segment	1,613	3,774	5,513	4,005	5,508	6,909	25	5,618	9,282	12,422	34
Coal segment	734	493	110	965	(149)	(1,626)	991	1,699	344	(1,516)	(541)
Chemical segment	100	(519)	(1,367)	8	(1,670)	(3,798)	127	108	(2,189)	(5,165)	136
Other segments	259	203	(158)	(63)	235	(358)	(252)	196	438	(516)	(218)
Elimination/adjustments	(338)	63	38	261	21	(91)	(527)	(77)	84	(53)	(163)
Income tax	(447)	(877)	(1,273)	(916)	(1,491)	(2,011)	35	(1,363)	(2,367)	(3,284)	39
Minority Interest	(767)	(1,117)	(834)	(1,395)	(1,071)	713	(167)	(2,162)	(2,189)	(121)	(94)
Profit attributable to shareholders	1,154	2,019	2,029	2,865	1,383	(261)	(119)	4,019	3,403	1,767	(48)
EPS	0.09	0.15	0.15	0.21	0.11	(0)	(121)	0.3	0.26	0.13	(50)
DPS	0	0	0	0.1	0.12	0	8	0.1	0.12	0.13	8
Net gearing	398%	411%	383%	399%	385%	391%	6	399%	385%	391%	6
Margin analysis											
EBITDA margin	28%	33%	38%	30%	34%	32%	(3)	29%	34%	35%	1
EBIT margin	16%	20%	23%	19%	21%	14%	(7)	17%	20%	19%	(2)
Net profit margin	3%	5%	6%	7%	4%	-1%	(4)	5%	5%	3%	(2)
Effective tax rate	19%	22%	31%	18%	38%	194%	156	18%	30%	63%	34
PBT margin by segment											
Power generation segment	5%	12%	18%	11%	16%	21%	4	8%	14%	19%	5
Coal segment	41%	20%	8%	23%	-8%	-513%	(505)	28%	8%	-86%	(94)
Chemical segment	7%	-29%	-97%	1%	-53%	-172%	(119)	4%	-44%	-143%	(98)
Other segments	91%	35%	-21%	-24%	-176%	102%	278	36%	97%	-129%	(226)

Power generation (GWh)	97,588	92,855	90,927	104,558	99,013	97,918	(1.11)	202,146	191,867	188,845	(1.58)
Unit fuel cost	209	170	151	179	155	140	(9.79)	194	162	145	(10.48)

Source: Company data, J.P. Morgan calculations.

Table 2: Quarterly results in 2014 under PRC GAAP (In RMB MM unless otherwise specify)

	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14	Y/Y	2013	2014	Y/Y
Turnover	18,413	18,597	18,503	19,714	17,512	17,331	17,470	17,881	(9)	75,227	70,194	(7)
COGS	(13,956)	(14,166)	(11,993)	(13,963)	(12,642)	(12,256)	(11,784)	(12,417)	(11)	(54,079)	(49,099)	(9)
Gross profit	4,457	4,431	6,510	5,751	4,870	5,075	5,686	5,464	(5)	21,149	21,095	(0)
Selling expenses	(133)	(130)	(105)	(179)	(63)	(121)	(183)	(156)	(13)	(546)	(523)	(4)
Administrative expenses	(587)	(612)	(1,100)	(1,293)	(651)	(929)	(970)	(2,020)	56	(3,593)	(4,570)	27
Others	(155)	(211)	(205)	(1,459)	(162)	(199)	(173)	(3,386)	132	(2,030)	(3,920)	93
EBIT	3,582	3,478	5,100	2,820	3,994	3,826	4,361	(98)	(103)	14,981	12,082	(19)
Financial cost	(2,023)	(2,020)	(1,998)	(2,235)	(2,090)	(2,102)	(2,154)	(2,270)	2	(8,276)	(8,616)	4
Investment income	276	384	201	284	41	199	568	159	(44)	1,144	967	(15)
Operating profit	1,834	1,843	3,303	869	1,945	1,923	2,774	(2,209)	(354)	7,849	4,434	(44)
Non-operating income/(loss)	54	154	121	(214)	63	150	149	417	(295)	115	778	574
EBT	1,889	1,997	3,424	655	2,008	2,073	2,923	(1,792)	(374)	7,964	5,212	(35)
Taxation	(485)	(390)	(834)	(660)	(645)	(620)	(658)	(1,363)	106	(2,369)	(3,286)	39
Minority interest	(466)	(656)	(804)	(268)	(421)	(420)	(580)	1,289	(581)	(2,194)	(128)	(94)
Net profit (reported)	938	950	1,786	(273)	943	1,032	1,685	(1,866)	583	3,401	1,798	(47)
Margins												
Gross margin	24%	24%	35%	29%	28%	29%	33%	31%	1.4	28%	30%	1.9
EBIT margin	19%	19%	28%	14%	23%	22%	25%	-1%	(14.9)	20%	17%	(2.7)
EBT margin	10%	11%	19%	3%	11%	12%	17%	-10%	(13.3)	11%	7%	(3.2)
Net profit margin	5%	5%	10%	-1%	5%	6%	10%	-10%	(9.0)	5%	3%	(2.0)

Source: Company data, J.P. Morgan calculations.

Investment Thesis

Datang International is one of the five major independent power producers in China, with total installed capacity of 39 GW as of Dec-13. Its power generation business is located in North China, Gansu, Jiangsu, Zhejiang, Yunnan, Fujian, Guangdong, Chongqing, Jiangxi, Liaoning, Xingxia and Qinghai. We rate Datang-H Neutral due to potential upside on the disposal of CTC assets and more upside from nuclear capacity, but downside on the tariff cut and lower-than-expected utilization

Valuation

Our Dec-15 PT of HK\$4.10 is based on DCF with a 10.1% WACC and a 2% terminal growth rate.

Risks to Rating and Price Target

Downside risks include potential tariff cuts. Upside risks include disposal of CTC assets and potential asset injection opportunities.

Independent Power Producer

AC

Boris Kan

(852) 2800-8573

boris.cw.kan@jpmorgan.com

Bloomberg JPMA KAN <GO>

Elaine Wu

(852) 2800-8575

elaine.wu@jpmorgan.com

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China Power International (2380.HK/HK\$3.96/Overweight)

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Date	Rating	Share Price (HK\$)	Price Target (HK \$)
17-Nov-06	N	3.40	6.90
02-Apr-07	N	3.91	7.45
30-May-07	N	4.90	7.90
13-Aug-07	N	5.81	5.61
28-Aug-07	N	8.94	7.90
12-Dec-07	N	7.37	7.50
13-Mar-08	N	4.75	5.30
27-Oct-08	N	2.79	4.50

19-Feb-09	N	3.70	4.10
17-Aug-09	N	4.70	4.50
23-Oct-09	N	4.03	4.30
06-Aug-10	N	3.34	3.20
22-Aug-10	N	3.18	3.40
15-Feb-11	N	2.68	3.00
29-Aug-11	N	2.07	2.50
22-Feb-12	UW	2.87	2.40
20-May-12	N	2.63	2.50
20-Aug-12	N	2.79	2.50
21-Aug-12	N	2.79	2.50
07-Feb-13	N	3.37	3.30
12-Jul-13	N	3.27	3.60
16-Oct-13	N	3.51	3.80
25-Apr-14	N	3.09	3.40
19-Dec-14	OW	4.04	5.20
11-Feb-15	N	3.60	4.10

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Date	Rating	Share Price (HK\$)	Price Target (HK\$)
06-Aug-10	N	1.70	1.86
15-Feb-11	N	1.55	1.60
22-Feb-12	N	2.06	2.10
24-Mar-12	N	1.68	2.00
20-May-12	N	1.66	2.10
20-Aug-12	N	2.18	2.10
07-Feb-13	N	2.84	2.70
21-Mar-13	N	2.48	2.70
12-Jul-13	OW	2.73	3.40
18-Aug-13	OW	2.87	3.90
16-Oct-13	OW	3.01	4.00
15-Aug-14	OW	3.24	4.20
19-Dec-14	OW	3.55	4.80
11-Feb-15	OW	3.72	4.60

<http://gps-app.emea.jpmchase.net:6080/server/console/chart/?shareClassId=1003493&shareClassServerId=4&chartDesignation=1&actionType=C>

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