

JPM-pp1

Asia Pacific Equity Research

20 March 2015

## China Resources Power Holdings (836 HK)

Neutral

Price: HK\$19.70

19 Mar 2015

Price Target: HK\$19.80

PT End Date: 31 Dec 2015

Core FY14 profits largely in line. But coal mine impairment provisions a concern

- **Core profits in line:** CR Power announced FY14 results yesterday. Stripping away non-core items (Table 2) of HK\$6.3B (e.g., impairment loss provisions (~HK\$7bn, mostly on coal mines), net of FV change on derivatives (HK\$594MM)), core pre-tax profits of HK\$17.5B represented a +1% Y/Y increase and was largely in line with consensus.
- **Impairment on coal mine assets:** Amongst the HK\$7B impairment provisions, HK\$5.8B/HK\$1.1B were related to consolidated coal mines and non-consolidated coal mines respectively. The impairment provisions were due to: 1) increase in initial investments in mines and the costs of subsequent technical upgrades of mines due to higher safety standards, 2) longer-than-expected construction period and COD delay, 3) falling coal price, and 4) temporary or full suspension of certain coal-mines. Management highlighted that most provisions made were for coal mines in Shanxi, while Daning (better coal quality) and Wujianfang (projects with real positive progress). While management did not disclose further financial details, the HK\$6-7B provisions represented (1) 14-16% of CRP's coal mine segmental assets and 17-20% of segmental net asset value as of Jun 2014 & (2) 8-10% of CRP's entire S/H equity and ~3 of total assets as of Dec 2014.
- **Potential tariff cut?** Management conceived the possibility of a potential tariff cut, but did not provide any guidance on the exact timing.
- **Unit fuel cost guidance:** Management is conservatively guiding for a 1% Y/Y decline, very conservative in our view given that average YTD coal prices are 3-5% below average levels last year.
- **Utilization guidance:** Management is guiding for a coal-fired utilization of 5,050 hours this year, down 5% Y/Y on a same plant basis. This is in line with the YTD run rate.
- **Direct power purchase** accounted for 4.7% of the company's total power generation output in 2014 and is expected to further increase to 5.8% this year. The company plays a very significant role in this space in certain provinces. For example, CRP accounted for 71% of direct power purchase in Henan last year. While no details were disclosed, management pointed out that marginal cash cost, rather than prevailing feed-in-tariffs, was the key decision factor in participating in direct power purchase.
- **Dividend payout** ratio increased to 40% in 2014 from 32% in 2013. Management sees more room for further upside in the future, although no exact timetable was provided.
- **Coal production** is expected to remain flattish Y/Y this year (2014: 11.6MM tons).
- **Net gearing** slightly increased to 130.2% as of Dec-14 from 125.7% at 2013YE .
- **NT downside:** Share price has underperformed the market by 5% YTD amidst market fears of potential tariff cut and potential utilization downside. The coal mine impairment provisions will likely add further downward pressure in the near term. 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).

Table 1: Summary of 2014 FY14 results (in HK\$MM)

(HK\$ m)	1H12	1H13	1H14	2H12	2H13	2H14	Y/Y	2012	2013	2014	Y/Y
Total net generation (GWh)	76,590	83,745	90,701	37,416	41,702	41,335	(1)	114,006	125,448	132,036	5
<b>Turnover</b>	<b>30,945</b>	<b>32,347</b>	<b>35,826</b>	<b>31,491</b>	<b>37,234</b>	<b>34,855</b>	(6)	<b>62,436</b>	<b>69,582</b>	<b>70,681</b>	2
Fuel Cost	(18,847)	(15,876)	(16,407)	(16,742)	(17,191)	(14,637)	(15)	(35,589)	(33,067)	(31,044)	(6)
Repair & Maintenance	(543)	(761)	(830)	(602)	(818)	(932)	14	(1,145)	(1,580)	(1,762)	12
Other income/ expenses	(3,381)	(3,918)	(6,168)	(4,093)	(6,142)	(7,293)	19	(7,474)	(10,060)	(13,460)	34
Total Cash Costs	(22,771)	(20,556)	(23,404)	(21,437)	(24,151)	(22,862)	(5)	(44,208)	(44,707)	(46,267)	3
<b>EBITDA</b>	<b>8,173</b>	<b>11,791</b>	<b>12,422</b>	<b>10,054</b>	<b>13,083</b>	<b>11,992</b>	(8)	<b>18,227</b>	<b>24,874</b>	<b>24,414</b>	(2)
Depreciation	(3,067)	(3,451)	(4,080)	(3,116)	(3,920)	(4,520)	15	(6,183)	(7,371)	(8,600)	17
<b>EBIT</b>	<b>5,106</b>	<b>8,340</b>	<b>8,342</b>	<b>6,938</b>	<b>9,163</b>	<b>7,472</b>	(18)	<b>12,044</b>	<b>17,503</b>	<b>15,814</b>	(10)
Finance Costs	(2,007)	(1,704)	(1,548)	(1,829)	(1,624)	(1,777)	9	(3,836)	(3,328)	(3,325)	(0)
Associate/JCE Results	765	1,062	584	968	898	(1,295)	(244)	1,734	1,961	(710)	(136)
Faire value change financial instruments	1	1	575	(39)	1	(1,169)	(116,763)	(38)	2	(594)	(39,072)
<b>EBT</b>	<b>3,865</b>	<b>7,699</b>	<b>7,953</b>	<b>6,039</b>	<b>8,439</b>	<b>3,231</b>	(62)	<b>9,904</b>	<b>16,137</b>	<b>11,184</b>	(31)
Taxation	(350)	(1,558)	(2,022)	(829)	(1,994)	(2,269)	14	(1,179)	(3,552)	(4,291)	21
Minority interests	(513)	(810)	133	(733)	(760)	2,189	(388)	(1,246)	(1,570)	2,321	(248)
<b>Net profit</b>	<b>3,002</b>	<b>5,331</b>	<b>6,064</b>	<b>4,477</b>	<b>5,685</b>	<b>3,151</b>	(45)	<b>7,479</b>	<b>11,016</b>	<b>9,215</b>	(16)
<b>EPS (Basic, HK\$)</b>	<b>0.63</b>	<b>1.13</b>	<b>1.28</b>	<b>0.96</b>	<b>1.19</b>	<b>0.66</b>	(45)	<b>1.59</b>	<b>2.32</b>	<b>1.94</b>	(16)
<b>DPS</b>	<b>0.06</b>	<b>0.08</b>	<b>0.08</b>	<b>0.45</b>	<b>0.67</b>	<b>0.70</b>	4	<b>0.51</b>	<b>0.75</b>	<b>0.78</b>	4
<b>Margins</b>											
EBITDA margin	26.4%	36.5%	34.7%	31.9%	35.1%	34.4%	(1)	29.2%	35.7%	34.5%	(1)
EBIT margin	16.5%	25.8%	23.3%	22.0%	24.6%	21.4%	(3)	19.3%	25.2%	22.4%	(3)
Net margin	9.7%	16.5%	16.9%	14.2%	15.3%	9.0%	(6)	12.0%	15.8%	13.0%	(3)
Effective tax rate	11.3%	23.5%	27.4%	16.4%	26.4%	50.1%	24	14.4%	25.1%	36.1%	11
Dividend Payout ratio	9.5%	7.1%	6.3%	47.0%	56.3%	106.1%	50	32.1%	32.3%	40.2%	8
<b>Segment analysis</b>											
Coal-fired power sales	28,424	28,323	31,594	26,985	32,231	31,003	(4)	55,409	60,553	62,597	3
Coal mining sales	2,520	2,324	1,960	2,023	3,065	1,541	(50)	4,543	5,389	3,500	(35)
Segment profit on coal-fired power	4,279	6,819	8,827	5,720	7,726	9,881	28	9,999	14,544	18,709	29
Segment profit on renewables	N/A	1,039	1,286	N/A	1,020	1,182	16	1,450	2,034	2,468	21
Segment profit on coal mining	798	688	(1,809)	(23)	(354)	(4,596)	1,199	775	334	(6,405)	(2,016)
Segment margin on coal-fire power	15.1%	24.1%	27.9%	21.2%	24.0%	31.9%	8	18.0%	24.0%	29.9%	6
Segment margin on coal mining	31.7%	29.6%	-92.3%	-1.1%	-11.5%	-298.3%	(287)	17.1%	6.2%	-183.0%	(189)

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

Table 2: CR Power - Core pre-tax profit reconciliation

HK\$ MM	2014	2013	Y/Y Chg (%)
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<b>PBT</b>	<b>11,184</b>	<b>16,137</b>	<b>-31%</b>
Impairment charge (mostly on consol. coal mines)	(6,094)	(1,997)	
Exchange loss	(114)	893	
Fair value changes on financial assets	2	(1)	
Fair value changes on derivative financial instruments (mainly a call option to buy additional 16% stake in Hezhou Power Plant)	594	(2)	
Gain on disposal of PPE	13	(108)	
Gain on disposal of prepaid lease payment	102	8	
Gain on disposal of equity investments	276	(20)	
Impairment charges on non-consol coal mines (included in share of associates)	(1,093)	-	
<b>Sub-total</b>	<b>6,314</b>	<b>1,227</b>	<b>+415%</b>
<b>Core PBT</b>	<b>17,498</b>	<b>17,364</b>	<b>+1%</b>

Source: J.P. Morgan estimates.

### Investment Thesis

China Resources Power is a flagship subsidiary of China Resources (Holdings) Company Limited, engaged in the investment, development, operation and management of power plants. As of 30 June 2014, the operational attributable installed capacity of CR Power was 30GW. We rate CRP Neutral due to potential downside on thermal utilization (coastal exposure) and coal mine business (falling production and ASP).

### Valuation

Our Dec-15 PT of HK\$19.80 is based on a 10-year DCF assuming a WACC of 8.4% and 2% terminal growth.

### Risks to Rating and Price Target

Upside risks to our rating and PT include further decreases in coal prices and utilization recovery. Downside risks include spot coal spiking up in light of temporary railway transportation disruption, and further IPP tariff cuts under the current coal-cost pass through mechanism.

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Date	Rating	Share Price (HK\$)	Price Target (HK\$)
03-Oct-06	N	8.09	7.80
17-Nov-06	N	10.53	11.20
30-May-07	N	14.34	12.20
20-Aug-07	N	16.44	18.00
05-Oct-07	N	25.93	29.50
12-Dec-07	N	27.60	28.60
13-Mar-08	N	15.08	16.00
31-Mar-08	N	13.98	18.10
02-Sep-08	N	18.13	16.10
04-Nov-08	N	13.95	18.50
24-Aug-09	N	18.78	21.20
06-Aug-10	OW	17.12	22.00
15-Feb-11	OW	12.92	18.50
18-Mar-11	OW	13.48	20.00
23-Aug-11	OW	13.70	16.90
22-Feb-12	OW	15.10	19.24
20-Mar-12	OW	15.22	18.10
20-May-12	OW	14.00	19.00
20-Aug-12	OW	16.38	18.60
07-Feb-13	OW	22.35	26.00
19-Mar-13	OW	20.95	28.00
13-May-13	N	22.85	23.30
31-May-13	NR	20.45	--
12-Aug-13	N	17.60	19.50
16-Oct-13	OW	19.34	23.50
05-Feb-14	OW	18.42	26.60
19-Aug-14	OW	22.20	28.50
19-Dec-14	N	19.74	22.50
11-Feb-15	N	19.92	19.80

<http://gps-app.emea.jpmchase.net:6080/server/console/chart/?shareClassId=503389&shareClassServerId=4&chartDesignation=1&actionType=C>

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