

Enn Energy (2688 HK)

Buy

Target price (HKD)	61.00
Share price (HKD)	46.05
Upside/Downside (%)	32.5

Dec	2013 a	2014 e	2015 e
HSBC EPS	1.79	2.00	2.31
HSBC PE	20.6	18.5	16.0
Performance	1M	3M	12M
Absolute (%)	11.0	4.7	-14.7
Relative ^A (%)	13.8	1.5	-29.5

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Buy: FY14 results, first take

- ▶ **FY14 net normalized attributable profit 2,491m vs HSBCe/Consensus: HKD2,162m/2,501m**
- ▶ **2H/FY14 volume 5.1/10.1bcm, +18/25.9% YOY, FY14 dollar margin RMB0.83/cm (flat YoY), FY15 volume growth guidance 20-25%**
- ▶ **Reiterate Buy, fair value TP HKD61.0 unchanged**

FY14 results. FY14 revenue/net normalized attributable profit is HKD29,087/2,491m vs HSBCe HKD32,016/2,162m (consensus: HKD2,501m), 2H/FY14e net attributable profit represents 52% (HSBCe: 45%). Dividend/share HKD0.66 vs HSBCe/consensus HKD0.74/0.645. Analyst briefing will be held after market on 31 March 2015.

2H/FY14 gas sales volume is 5.1/10.1bcm, +18%/25.9% YoY (vs 1H14: 33%). ENN Energy has reduced supply to some ceramics producers with lower dollar margin and safety issues for Quanzhou project (2H gas sales volume lower than 1H). However, overall dollar margin is higher because less of the gas volume is to be supplied by gas supply outside of long-term contracts, which are on average cRMB1/cm more expensive. Wholesale gas c8% of total volume (vs c4.5/7.3% in FY13/1H14).

FY14 dollar margin (ex-wholesale) was RMB0.83/cm (vs 1H14: RMB0.76/cm; FY13: RMB0.83/cm). With the September 2014 citygate price hike passthrough, the increased VWAP gas cost due to higher incremental gas volume was also passed through to the end users.

Other details: a) FY14 Opex/revenue was 8% vs 9% with better costs control; b) ENN Energy is currently distributing gas to c70 gas refuelling station for Sinopec Marketing, the company looks to increase cooperation with the company; c) FY14 CNG dollar margin cRMB1.1/cm (vs FY13 RMB1.2/cm).

Preliminary FY15 guidance: a) 20-25% volume growth (include wholesale gas), b) Capex: RMB3-3.5bn; c) No. of new connections: 1.3-1.4m; d) CNG/LNG stations build-out: 20/60; e) 20% core earnings growth. f) ENN US/Canada to breakeven in 2H16.

We look for more information about: a) potential margin erosion with more wholesale gas, b) volume growth by segment, c) details about opex control and target FY15 opex/revenue; d) ENN US/Canada operational data, e) outlook for ship bunkering, cooperation with Sinopec management.

Index ^A	HSCEI	Enterprise value (CNYm)	46,536
Index level	11,920	Free float (%)	69
RIC	2688.HK	Market cap (USDm)	6,432
Bloomberg	2688 HK	Market cap (HKDm)	49,875

Source: HSBC

Source: HSBC

Investment thesis. ENN Energy shares appear undervalued (trading below the 3-year historical average PE of 22x) although we believe the company offers more robust EPS growth than its peers. Although China is expected to see a slowing economy and a low oil price environment, we continue to like ENN Energy, as we believe it can still deliver above-industry average volume growth in challenging times.

Valuation and risks. We derive our fair value target price of HKD61.0 by an equal-weighted average of three methods: PE, PB, and DCF. Our PE-based valuation of HKD57.75 per share uses a multiple of 20.0x 2015e EPS, based on 1x 2015e-17e PEG. Our PB valuation of HKD54.54 per share is based on an ROE-implied 2015e PB of 3.5x. Our DCF valuation of HKD71.44 per share assumes a WACC of 6.5%, a risk-free rate of 3.5%, an equity risk premium of 5.5%, and a beta of 0.67. We establish a Buy rating for the stock.

Downside risks: (1) a decline in industrial volumes with slowing GDP and (2) any future citygate price hikes not being passed through to customers.

Disclosure appendix

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From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

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Upside/Downside is the percentage difference between the target price and the share price.

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For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

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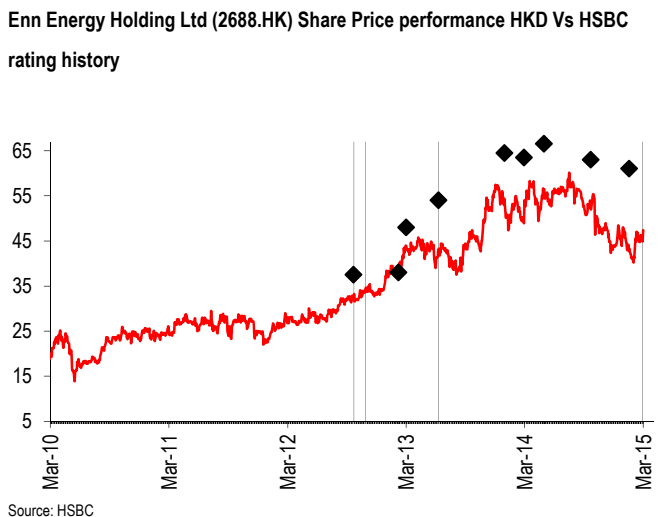
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Hold	39%	(28% of these provided with Investment Banking Services)
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For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see “Stock ratings and basis for financial analysis” above.

Share price and rating changes for long-term investment opportunities



Recommendation & price target history		
From	To	Date
N/A	Overweight	16 October 2012
Overweight	Neutral	22 November 2012
Neutral	Overweight	04 July 2013
Overweight	Buy	25 March 2015
Target Price	Value	Date
Price 1	37.50	16 October 2012
Price 2	38.00	03 March 2013
Price 3	48.00	27 March 2013
Price 4	54.00	04 July 2013
Price 5	64.50	24 January 2014
Price 6	63.50	25 March 2014
Price 7	66.50	25 May 2014
Price 8	63.00	16 October 2014
Price 9	61.00	12 February 2015

Source: HSBC

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
ENN ENERGY HOLDINGS LTD	2688.HK	47.35	27-Mar-2015	1, 5, 6, 7

Source: HSBC

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