

Gas Utilities	Last Close	Target Price	Upside	20 April 2018
	HK\$27.50	HK\$31.00↑	+12.7%	

## China Gas Holdings (384 HK)

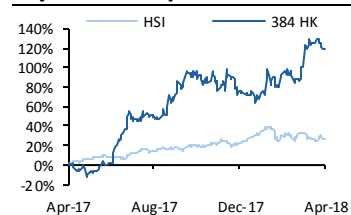
### Expect a strong finish in FY18; lift TP

- ⊕ **Strong momentum in gas sales sustained in Jan-Mar 2018:** We maintain our positive stance on CGH's growth prospect after a recent update with management. We expect CGH to have maintained strong momentum in retail gas sales during Jan-Mar this year with ~35% YoY growth after posting ~37% YoY growth during 10MFY18 period. Therefore, we are comfortable to uphold our FY18 forecast of ~36% YoY growth in retail gas sales and 53% YoY growth in total gas sales. Management maintained the guidance of 25% YoY growth in retail gas sales for FY19E and FY20E. Regarding dollar margin, we maintain our forecasts of RMB0.62/m<sup>3</sup> for 2HFY18 and RMB0.63/m<sup>3</sup> for full-year FY18.
- ⊕ **New connections to stay robust in FY19E:** We estimate CGH to complete 1.1m rural new connections in FY18, thanks to its strong execution of coal-to-gas conversion campaign in 2017. Management explained that the rural new connections were mainly in Hebei and Tianjin in FY18E. Together with 2.7m from urban areas, total new residential connections should reach 3.8m in FY18E. Management maintained FY19E rural area connection target of 2.0m, which will further extend from Hebei and Tianjin to Shandong, Shanxi and Henan.
- ⊕ **Investment in gas storage facilities not likely to speed up in short term:** Meanwhile, management guided for at least HK\$6.5bn capex to be spent in FY19E. Investment in rural coal-to-gas conversion and urban projects will be split into around 1:1. Currently, management stated that CGH does not have plans to speed up investment in gas storage facilities, before the company could see satisfactory investment returns.
- ⊕ **Valuation justified on higher growth; maintain Buy:** After fine-tuning our model, we lift our FY19/20E earnings by 2.2%/2.9% to factor in RMB appreciation against HKD and more stable dollar margin forecasts after FY20E. We also revise up our DCF-based TP to HK\$31.00 (from HK\$28.00). In our view, CGH's highest gas sales and net profit growth could justify its higher valuation at 18x forward P/E vs. ENN (2688 HK) and CR Gas (1193 HK) (trading at ~14x/16x forward P/E). Maintain **Buy**.

### Stock Rating

**BUY**

### 1-year stock performance



Source: Bloomberg

### Stock data

52w high (HK\$)	29.70
52w low (HK\$)	10.44
Market cap (HK\$ m)	136,634
Avg daily vol (m)	5.62
YTD change (%)	27.3
200d MA (HK\$)	22.50

Source: Bloomberg

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### Financial highlights

Y/E 31 Mar	2016	2017	2018E	2019E	2020E
Revenue (HK\$ m)	29,497	31,993	43,810	55,544	66,924
YoY growth (%)	1.2	8.5	36.9	26.8	20.5
Net profit (HK\$ m)	2,273	4,148	6,260	7,573	8,839
EPS (HK\$)	0.46	0.83	1.26	1.52	1.78
YoY growth (%)	1.9	80.3	50.9	21.0	16.7
Previous EPS (HK\$)			1.26	1.49	1.73
Change (%)			0.0	2.2	2.9
P/E (x)	59.4	32.9	21.8	18.0	15.5
BVPS (HK\$)	3.64	4.14	5.12	6.26	7.57
P/B (x)	7.6	6.6	5.4	4.4	3.6
Dividend yield (%)	0.7	0.9	1.4	1.6	1.9

Source: Company data, BOCOM Int'l estimates

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**Figure 1: DCF model**

(HK\$ m) / Y/E 31 Dec	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E	2027E	2028E
Year	1	2	3	4	5	6	7	8	9	10
Cash from operations	9,389	11,390	12,814	14,476	15,805	17,584	19,395	21,605	24,213	27,750
Less: Capex	(6,508)	(6,874)	(6,972)	(6,813)	(6,659)	(6,511)	(6,368)	(6,083)	(5,953)	(5,690)
<b>Free cash flow</b>	<b>2,881</b>	<b>4,516</b>	<b>5,841</b>	<b>7,663</b>	<b>9,146</b>	<b>11,073</b>	<b>13,027</b>	<b>15,522</b>	<b>18,261</b>	<b>22,060</b>

Terminal growth rate (%) 1.5

Sum of PV of FCF 60,041

Terminal value 114,693

Less: Net cash/(debt) (2018E) (15,391)

Less: MI (2018E) (5,479)

**Equity value (HK\$ m) 153,865**

Total no. of shares (m) 4,969

**Equity value per share (HK\$) 31.00**

WACC Derivation	
Risk free rate	3.3
Market risk premium	10.0
Beta	0.95
Cost of equity	12.8
Pre-tax cost of debt	4.1
Effective tax rate	19.0
After-tax cost of debt	3.3
Estimated debt ratio	35.5
<b>WACC</b>	<b>9.4</b>

Source: BOCOM Int'l estimates

**Figure 2: DCF valuation sensitivity analysis**

g / WACC	8.5%	9.0%	9.5%	10.0%	10.5%
0.5%	33.7	30.8	28.2	25.9	23.9
1.0%	35.5	32.3	29.5	27.0	24.8
1.5%	37.6	34.0	<b>31.0</b>	28.3	25.9
2.0%	40.0	36.0	32.6	29.7	27.1
2.5%	42.8	38.3	34.6	31.3	28.5

Source: BOCOM Int'l estimates

**Figure 3: Forward P/E band (x)**

Source: Bloomberg, BOCOM Int'l estimates

**Figure 4: Forward P/B band (x)**

Source: Bloomberg, BOCOM Int'l estimates

20 April 2018

**China Gas Holdings (384 HK)****Financial Statements**

Income statement (HK\$ m)					
Y/E 31 Mar	2016	2017	2018E	2019E	2020E
Turnover	29,497	31,993	43,810	55,544	66,924
COGS	(22,283)	(23,616)	(32,346)	(41,250)	(50,225)
<b>Gross profit</b>	<b>7,214</b>	<b>8,377</b>	<b>11,464</b>	<b>14,293</b>	<b>16,699</b>
Other income	486	446	536	626	713
Other income and gains	(959)	(215)	0	0	0
Selling and distribution expenses	(1,088)	(1,229)	(1,665)	(2,222)	(2,677)
Administrative expenses	(1,561)	(1,675)	(2,191)	(2,777)	(3,279)
<b>Operating profit</b>	<b>4,092</b>	<b>5,703</b>	<b>8,144</b>	<b>9,920</b>	<b>11,456</b>
Net finance costs	(758)	(705)	(780)	(819)	(694)
Share of results of associates	185	293	346	380	418
Share of results of joint ventures	198	611	1,192	1,287	1,390
<b>Pre-tax profit</b>	<b>3,718</b>	<b>5,902</b>	<b>8,902</b>	<b>10,769</b>	<b>12,571</b>
Income tax expense	(984)	(1,208)	(1,691)	(2,046)	(2,388)
<b>After tax profit</b>	<b>2,733</b>	<b>4,695</b>	<b>7,211</b>	<b>8,723</b>	<b>10,182</b>
Minority interest	(460)	(547)	(951)	(1,150)	(1,343)
<b>Net profit</b>	<b>2,273</b>	<b>4,148</b>	<b>6,260</b>	<b>7,573</b>	<b>8,839</b>

Balance sheet (HK\$ m)					
As of 31 Mar	2016	2017	2018E	2019E	2020E
Cash & cash equivalent	5,497	4,725	8,900	11,143	10,641
Inventories	1,213	1,679	2,215	2,825	3,440
Amounts due from customers	1,136	1,738	1,917	2,507	3,163
Trade and other receivables	5,094	6,067	8,042	10,196	11,918
Other current assets	706	1,154	1,154	1,154	1,154
<b>Total current assets</b>	<b>13,647</b>	<b>15,363</b>	<b>22,229</b>	<b>27,825</b>	<b>30,316</b>
Property, plant & equipment	22,850	25,783	30,261	35,168	40,265
Investments in associates	3,833	4,166	4,886	5,641	6,434
Investments in joint ventures	5,070	5,412	6,629	7,942	9,358
Intangible assets	3,060	3,003	3,009	3,013	3,014
Other non-current assets	5,073	6,260	6,260	6,260	6,260
<b>Total non-current assets</b>	<b>39,886</b>	<b>44,624</b>	<b>51,046</b>	<b>58,024</b>	<b>65,332</b>
Short-term borrowings	10,324	10,873	14,020	14,721	13,249
Trade and other payables	8,549	9,650	14,622	18,647	22,705
Amounts due to customers	525	645	884	1,164	1,417
Other current liabilities	404	1,411	1,483	1,668	1,992
<b>Total current liabilities</b>	<b>19,803</b>	<b>22,579</b>	<b>31,008</b>	<b>36,200</b>	<b>39,362</b>
Long-term borrowings	12,010	12,745	11,743	12,330	11,097
Other non-current liabilities	756	735	735	735	735
<b>Total non-current liabilities</b>	<b>12,766</b>	<b>13,480</b>	<b>12,478</b>	<b>13,065</b>	<b>11,832</b>
Share capital	49	50	50	50	50
Reserves	17,803	20,501	25,411	31,056	37,583
Equity attri. to shareholders	17,853	20,550	25,460	31,105	37,632
Non-controlling interests	3,112	3,377	4,328	5,479	6,821
<b>Total equity</b>	<b>20,964</b>	<b>23,928</b>	<b>29,789</b>	<b>36,584</b>	<b>44,454</b>

Source: Company data, BOCOM Int'l estimates

Cash flow statement (HK\$ m)					
Y/E 31 Mar	2016	2017	2018E	2019E	2020E
Pre-tax profit	3,718	5,902	8,902	10,769	12,571
Tax paid	(992)	(1,102)	(1,620)	(1,861)	(2,064)
Depreciation & amortization	914	960	1,033	1,197	1,375
Change in working capital	1,193	(1,473)	2,521	952	1,317
Others	1,030	(170)	(1,538)	(1,668)	(1,809)
<b>Cash from operations</b>	<b>5,862</b>	<b>4,116</b>	<b>9,299</b>	<b>9,389</b>	<b>11,390</b>
Capital expenditure	(3,157)	(2,754)	(4,470)	(4,992)	(5,285)
Others	(845)	(1,358)	(1,448)	(1,515)	(1,589)
<b>Cash from investing</b>	<b>(4,001)</b>	<b>(4,112)</b>	<b>(5,918)</b>	<b>(6,508)</b>	<b>(6,874)</b>
Proceed of issue of shares	0	0	0	0	0
Change in borrowing	23,035	18,516	2,144	1,288	(2,705)
Dividends paid	(942)	(954)	(1,350)	(1,927)	(2,313)
Others	(23,420)	(18,082)	0	0	0
<b>Cash from financing</b>	<b>(1,327)</b>	<b>(520)</b>	<b>794</b>	<b>(639)</b>	<b>(5,018)</b>
FX change	(265)	(256)	0	0	0
<b>Net change in cash</b>	<b>268</b>	<b>(772)</b>	<b>4,176</b>	<b>2,242</b>	<b>(502)</b>

Financial ratios					
Y/E 31 Mar	2016	2017E	2018E	2019E	2020E
Gross margin (%)	24.5	26.2	26.2	25.7	25.0
EBIT margin (%)	13.9	17.8	18.6	17.9	17.1
Net margin (%)	7.7	13.0	14.3	13.6	13.2
ROA (%)	4.2	6.9	8.5	8.8	9.2
ROE (%)	12.7	20.2	24.6	24.3	23.5
Net gearing (%)	92.8	89.4	64.2	49.5	35.0
Interest coverage (x)	5.4	8.1	10.4	12.1	16.5
Current ratio	0.7	0.7	0.7	0.8	0.8

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**Buy:** The stock's total return is expected to **exceed** that of the corresponding industry over the next 12 months.

**Neutral:** The stock's total return is expected to be **in line with** that of the corresponding industry over the next 12 months.

**Sell:** The stock's total return is expected to be **below** that of the corresponding industry over the next 12 months.

**Not-Rated:** The analyst **does not have conviction** regarding the outlook of the stock's total return relative to that of the corresponding industry over the next 12 months.

#### Analyst Industry Views:

**Outperform:** The analyst expects the industry coverage universe to be **attractive** relative to the relevant broad market benchmark over the next 12 months.

**Market perform:** The analyst expects the industry coverage universe to be **in line with** the relevant broad market benchmark over the next 12 months.

**Underperform:** The analyst expects the industry coverage universe to be **unattractive** relative to the relevant broad market benchmark over the next 12 months.

Broad market benchmark for Hong Kong is **the Hang Seng Composite Index**, for China A-shares is the **MSCI China A Index**, for US-listed Chinese companies is **S&P US Listed China 50 (USD) Index**.

20 April 2018

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