

Results Update

China Everbright International

0257 HK

Another fruitful year to come

- CEI recorded net profit attributable to shareholders of HKD1,324.7m in FY12/13, a YoY increase of 50.3%.
- We believe WTE business will continue to lead growth because 11 WTE projects will commence construction this year and will become operational in 2015.
- We think the transaction between CEI and HanKore will be beneficial to the company because of the synergies between their businesses and its potential to realize the value of its water treatment business by spinning it off on the Singapore market.
- We revised our TP from HKD8.0 to HKD10.8 based on our expectation of higher free cash flow in coming years.

Nelson Lee, CFA, FRM

(852) 2533 3708

sbie2research@sbie2capital.com

Stock Data (257 HK)

Rating	HOLD
Price (HK\$)	11.72
Target Price (HK\$)	10.8
12m Price Range (HK\$)	4.95-12.12
Market cap. (HK\$m)	52,549.1
Daily t/o (HK\$m)	256.3
Free float (%)	60.3

Source: Bloomberg

What's New: China Everbright International (CEI) announced its year-end results for FY12/13. For the period, the company recorded total revenue of HKD5,319.9m, representing a YoY increase of 56.0%. The increase was mainly driven by the increase of construction income from waste-to-energy (WTE) projects, which was up 169.8% YoY. Operating income was up by 43.4% YoY to HKD2,127.2m, and net profit attributable to shareholders was up by 50.3% YoY to HKD1,324.7m, in line with the market expectation of HKD1320.8m. The company proposed a final dividend of HK5.0 cents per share, making the full year dividend HK8.5 cents per share, representing a payout ratio of 26.1% (FY12/12: 20.2%).

On the back of more environmental projects this year, we revised the turnover and net profit upward for the next few years as we expect construction revenue and operating revenue to see significant improvements. We also revised our target price on CEI upward from HKD8.0 to HKD10.8 based on our expectation of higher free cash flow generated by more environmental projects.

However, because CEI's share price has already seen significant increases, rising by 164.0% by year-end last year and by 12.9% year-to-date, we see limited upside for its share price at this moment. We therefore downgrade it from BUY to HOLD.

Figure 1: Financials and Valuation

	FY12/12	FY12/13	FY12/14E	FY12/15E	FY12/16E
Total Revenue (HKD mn)	3,410	5,320	7,843	8,967	5,685
Revenue Growth(YoY)	-2.2%	56.0%	47.4%	14.3%	-36.6%
EBIT (HKD mn)	1,483	2,127	2,709	3,340	3,056
EBIT Growth(YoY)	17.7%	43.4%	27.4%	23.3%	-8.5%
Net Profit (HKD mn)	1,123	1,325	1,679	2,105	1,893
Net Profit Growth(YoY)	40.2%	17.9%	26.7%	25.4%	-10.1%
EPS (HKD)	0.30	0.30	0.37	0.47	0.42
DPS (HKD)	0.06	0.09	0.07	0.09	0.08
P/E (x)	39.80	39.94	31.51	25.13	27.95
Dividend Yield	0.5%	0.7%	0.6%	0.8%	0.7%

Source: The company

Figure 2: Revenue breakdown for FY12/13

	FY12/13 HKD'000	FY12/12 HKD'000	YoY Change
WTE projects			
construction revenue	2,516,997	932,978	169.8%
operation revenue	635,427	453,654	40.1%
sub total	3,152,424	1,386,632	127.3%
WTT projects			
construction revenue	449,779	530,231	-15.2%
operation revenue	558,461	502,789	11.1%
sub total	1,008,240	1,033,020	-2.4%
Alternative energy projects			
construction revenue	150,804	138,741	8.7%
operation revenue	259,867	256,097	1.5%
sub total	410,671	394,838	4.0%
Finance income	744,386	594,994	25.1%
rentals from investment properties	3,742	454	724.2%
Other	403	0	N.A
Total	5,319,866	3,409,938	169.8%

Source: The company

Waste-to-energy projects continued to lead growth: Revenue generated from WTE projects was up 127.3% YoY to HKD3,152.4m and contributed ~56.3% of total EBITDA of the company during the year (FY12/12: 52.5%). We believe this segment will continue to lead growth because: First, the 11 WTE projects that are in their preparatory stages will commence construction this year, with the total investment amounting RMB5,352.2m. Construction revenue in this segment is therefore expected to increase significantly in the coming years. We forecast it will increase by 101.0% to HKD5,064.9m in FY12/14, and will further increase to HKD5,801.2m in FY12/15.

Second, most projects under construction and in their preparatory stages will become operational in 2015, and therefore will boost operating revenue in the years that follow. We forecast these projects will contribute ~RMB542.3m operational cash flow to the company upon the completion of construction, and the revenue from operating revenue in this segment will increase by 32.0% YoY to HKD841.0m in FY12/14, further increasing to HKD1,147.6m in FY12/15.

Currently the company has 11 operational WTE projects, with total daily processing capacity of 10,650 tons. Upon the completion of the WTE projects currently under construction or in their preparatory stages, we believe the number of operational WTE projects and their total daily processing capacity will increase to 26 and 22,550 tons respectively.

Figure 3: WTE project pipeline

Project	Type of Investment	Concession right period	Total Investment (RMB)	Date of commercial operation	Daily processing capacity (ton)	Average annual power generation (kWh)
Operating projects						
Suzhou WTE Project Phase I	BOT	28	489,443,000	Jul-2006	1,050	100,000,000
Suzhou WTE Project Phase II	BOT	28	450,000,000	Jun-2009	1,000	100,000,000
Yixing WTE Project Phase I	BOT	28	238,300,000	Jun-2007	500	44,000,000
Jiangyin WTE Project Phase I	BOT	30	388,740,000	May-2008	800	77,000,000
Jiangyin WTE Project Phase II	BOT	27	205,000,000	Oct-2010	400	38,000,000
Changzhou WTE Project	BOT	25.5	412,560,000	Nov-2008	800	77,000,000
Zhenjiang WTE Project	BOT	30	413,338,000	Aug-2011	1000	100,000,000
Jinan WTE Project	BOT	25	900,920,000	Oct-2011	2000	190,000,000
Suqian WTE Project	BOT	30	324,152,000	Dec-2011	600	60,000,000
Suzhou WTE Project Phase III	BOT	28	750,000,000	Jan-2013	1500	158,000,000
Ningbo Beilun WTE Project Phase I	BOT	30	560,000,000	Jan-2014	1000	112,323,000
Total			5,132,453,000		10,650	1,056,323,000

Under construction

Nanjing WTE Project	BOT	30	1,030,218,000	1H2014	2000	220,000,000
Pizhou WTE Project Phase I	BOT	30	329,800,000	1H2014	600	71,000,000
Sanya WTE Project Phase I	BOT	27	425,646,000	2H2015	700	75,000,000
Shouquanq WTE Project Phase I	BOT	26	388,531,000	2H2014	600	80,000,000
Total			2,174,195,000		3,900	446,000,000

In preparatory stage

Huidong WTE Project	BOT	29	334,405,000	2H2015	600	104,000,000
Yixing WTE Project Phase II	BOT	28	150,843,000	2H2015	300	31,000,000
Wujiang WTE Project	BOT	30	890,000,000	2H2015	1,500	146,000,000
Boluo WTE Project Phase I	BOT	30	416,959,000	2H2015	700	91,360,000
Weifang WTE Project Phase I	BOT	30	586,000,000	2H2015	1,000	122,000,000
Ningbo Ninghai WTE Project Phase I	BOT	28	360,000,000	2H2015	700	90,000,000
Rizhao Project	BOT	25	350,000,000	2H2015	600	80,000,000
Heze City WTE Project Phase I	BOT	30	350,000,000	2H2015	600	80,000,000
Zhenjiang WTE Project Phase II	BOT	30	200,000,000	2H2015	400	45,000,000
Ma'anshan WTE Project Phase I	BOT	30	450,000,000	2H2015	800	100,000,000
Yiyang WTE Project	BOT	30	372,000,000	2H2015	800	90,000,000
Total			4,460,207,000		8,000	979,360,000

Source: The company

Expanding business into inland areas: Historically most of the company's WTE projects are located in coastal provinces like Jiangsu, Shandong, Guangdong, Zhejiang, and Hainan. These areas have relatively more developed economies and higher population densities compared to other regions in China. In FY12/13, the company started to expand its business in Inland areas including Hunan Yiyang and Anhui Ma'anshan. While it is good to see the company penetrating into a new market, we are uncertain as to whether the inland projects can yield similar returns to coastal projects, because: 1) local governments in coastal regions are generally richer and therefore more generous in paying waste treatment fees (currently RMB50-70/ton); 2) waste collection systems in inland regions are less developed, therefore it will be harder for the company to collect waste; and 3) heat value of the sold waste in inland regions is generally lower, the electricity generated from the waste in those area is therefore less.

Having said that, the management expressed that the construction expenses on the inland projects are much lower than those on the coastal areas, and therefore the IRR of those projects will not have a significant difference compared with coastal projects. We will keep a close eye on the performance of the two inland projects this year in order to get more information before making any judgment.

Expanding water treatment business by acquiring HanKore

In Dec 2013, CEI announced that it entered into a frame agreement with HanKore, a Singapore listed company engaged in water treatment business in China. Under the agreement, CEI will inject all of its water treatment businesses into HanKore, and HanKore will issue some of its shares to CEI in return. It is expected that CEI will hold more than 50.0% of the enlarged share capital of HanKore upon the completion of the transaction.

The water treatment business in CEI has slowed down this year due to less revenue from the construction of water treatment plants. However, we believe the transaction with HanKore will be beneficial to its future development, because 1) Similar to CEI, HanKore's water treatment businesses are also located in coastal areas including Jiangsu and Shandong. We believe there will be synergy between their businesses, when the assets are pool together and are utilized more efficiently. HanKore can also leverage on the strong SOE background of CEI, which would enable it to lower their financing costs of their projects (Borrowing costs of HanKore is ~8.0%, while that of CEI is ~5.0%); 2) In addition, CEI can realise the value of its water treatment business by spinning it off on the Singapore market, which should be positive to the equity value to the company.

CEI is in the process of conducting due diligence on HanKore, therefore our financial model has not factored in the acquisition. However, we will issue an update after it closes the deal.

Figure 4: WWT project pipeline

Project	Type of investment	Concession right period	Total investment (RMB)	Date of commercial operation	Daily average waste water treatment/ water supply capacity (m3)
Operating projects					
Qingdao Waste Water Treatment Project (Haibohe & Maidao Plants)	BOT/TOT	25	356,000,000	Jan-2005	220,000
Zibo Waste Water Treatment Project (Southern and Northern Plants)	TOT	25	354,276,000	Nov-2005	250,000
Zibo High-tech Zone Waste Water Treatment Project	BOT	25	150,000,000	Sep-2007	100,000
Zibo Zhoucun Waste Water Treatment Project	BOT	25	70,000,000	Nov-2009	40,000
Binzhou Boxing Waste Water Treatment Project	TOT/BOT	25	85,000,000	Phase I –April 2008 Phase II –June 2009	60,000
Jinan Waste Water Treatment Project (Plant 1 and Plant 2)	TOT	30	707,000,000	Nov-2006	500,000
Jinan Licheng Waste Water Treatment Project (Plant 3) Phase I	BOT	28	138,000,000	Oct-2009	100,000
Jinan Xike Waste Water Treatment Project (Plant 4)	BOT	26	72,680,000	Jun-2010	30,000
Ling County Waste Water Treatment Project (Plant 2)	BOT	30	58,000,000	Jun-2010	30,000
Ling County Waste Water Treatment Project (Plant 1)	TOT	30	33,720,000	Jun-2010	30,000
Jiangyin Waste Water Treatment Project (Acquisition and upgrade)	TOT	30	530,266,000	Jan-2008	190,000
Zibo Reusable Water Project Phase I	BOO	20	44,000,000	Sep-2011	4,800
Jinan Licheng Reusable Water Project	BOO	24	31,061,000	Sep-2011	42,000
Jiangyin Reusable Water Project	BOO	25	73,067,000	Jan-2013	10,000
Dezhou Nanyunhe Waste Water Treatment Project Phase I	BOT	25	150,270,000	End 2012	75,000
Jinan Licheng Waste Water Treatment Project	BOT	28	195,000,000	Nov-2013	100,000
Total			3,048,340,000		1,781,800
Transferred projects					
Xinyi BT Waste Water Treatment Project Phase I	BT	4	62,150,000	Oct-2010	10,000
Xinyi Surface Water BT Project	BT	8	385,110,000	Jan-2013	100,000
Total			447,260,000		110,000
Under construction					
Zhangjiu WWT Project	BOT	30	60,700,000	2014 (expected)	30,000
Total			60,700,000		30,000
In preparatory stage					
Ling County WWT Project (Plant 1) Upgrading	BOT	30	14,313,500	2015 (expected)	30,000
Dezhou Nanyunhe Waste Water Treatment Project Phase II	BOT	25	79,977,000	2014 (expected)	75,000
Zibo Reusable Water Project Phase II*	BOO	20	11,000,000	2014 (expected)	4,800
Total			105,290,500		109,800

Source: The company

Valuation: As CEI has secured more environmental projects this year, we revised the turnover and net profit upward for the next few years as we expect construction revenue and operating revenue will see significant improvements. It is worth noting that we conservatively forecast revenue in FY12/16 to be lower than that in FY12/15, as we assume there will only be 3 WTE projects start construction during the year (while there are 15 WTE projects under construction or in preparatory stages in FY12/14), and we expect the revenue from construction will be significantly lower than that in FY12/15.

We also revised upward our target price on CEI from HKD8.0 to HKD10.8 based on our expectation of higher free cash flow generated from more environmental projects. Our target price is derived from our DCF model which assumes weighted average cost of capital (WACC) of 7.5% and a terminal growth rate of 3.0%. However, because CEI's share price has already seen significant increases, rising by 164.0% by year-end last year and by 12.9% year-to-date, we see limited upside for its share price at this moment. We therefore downgrade it from BUY to HOLD.

Figure 5: DCF model

	FY12/14E	FY12/15E	FY12/16E	FY12/17E	FY12/18E	FY12/19E	FY12/20E
WACC@8.20%							
FCFF (HKD mn)	-631	-2,860	2,827	3,836	2,274	3,121	3,107
Discount Factor	0.930	0.864	0.80	0.75	0.69	0.64	0.60
Discounted FCFF (HKD mn)	-587	-2,471	2,270	2,864	1,577	2,013	1,863
PV of estimated FCFF (HKD mn)	7,529						
PV of terminal FCFF (HKD mn)	41,852						
Value of Firm (HKD mn)	49,381						
Minus: debt (HKD mn)			6,921				
Plus: cash and cash equivalent (HKD mn)			5,771				
Value of Equity (HKD mn)			48,231				
Total Shares outstanding (mn)			4,484				
Equity Value per share (HKD)			10.76				

Source: The company, SBI E2-Capital

Risks: Major risks include: 1) Cancellation of favorable government policies; 2) delays or slowdowns in construction progress; 3) reduction in utilization rate; 4) intense competition for new projects; 5) increases in interest rates raising borrowing costs; and 5) future placements that may dilute existing shareholders.

Figure 6: Per share items

	FY12/12	FY12/13	FY12/14E	FY12/15E	FY12/16E
EPS (HKD cents)					
-basic	29.7	29.5	37.4	47.0	42.2
-diluted	29.5	29.5	37.4	47.0	42.2
DPS (HKD cents)	6.0	8.5	7.5	9.4	8.4
BVPS (HKD)	1.9	3.1	3.4	3.8	4.1

Source: The company, SBI E2-Capital

Figure 7: Ratio analysis

	FY12/12	FY12/13	FY12/14E	FY12/15E	FY12/16E
Growth (YoY)					
revenue	-2.2%	56.0%	47.4%	14.3%	-36.6%
Gross profit	17.1%	41.1%	27.3%	22.4%	-11.2%
Operating profit	17.7%	43.4%	27.4%	23.3%	-8.5%
Net profit (including discontinued operation)	36.5%	18.2%	28.0%	25.4%	-10.1%
Net Profit from continuing operation	18.2%	50.9%	28.0%	25.4%	-10.1%
Margins					
Gross margin	49.4%	44.7%	38.5%	41.2%	57.8%
EBIT margin	43.5%	40.0%	34.5%	37.2%	53.8%
Net profit margin (excluding discontinued operation)	26.5%	25.6%	22.3%	24.4%	34.6%
Other Ratios					
Return on average assets	7.6%	6.8%	6.9%	7.6%	6.6%
Return on average equity	15.1%	12.2%	12.1%	13.6%	11.1%
dividend payout ratio	20.2%	28.8%	20.0%	20.0%	20.0%
Valuation Measures					
P/E (x)	23.9	24.0	18.9	15.1	16.8
P/B (x)	3.7	2.3	2.1	1.9	1.7
Dividend yield	0.8%	1.2%	1.1%	1.3%	1.2%

Source: The company, SBI E2-Capital

Figure 8: Income statement

	FY12/12	FY12/13	FY12/14E	FY12/15E	FY12/16E
Revenue	3,410	5,320	7,843	8,967	5,685
Cost of Sales	(1,726)	(2,944)	(4,820)	(5,268)	(2,401)
Gross Profit	1,684	2,375	3,023	3,699	3,284
Other income	97	144	235	269	171
Administrative costs	(297)	(392)	(549)	(628)	(398)
Profit from operation	1,483	2,127	2,709	3,340	3,056
Finance costs	(313)	(316)	(467)	(528)	(519)
Profit before taxation	1,171	1,812	2,242	2,812	2,537
Income tax	(267)	(447)	(496)	(622)	(569)
Profit from continuing operation	904	1,364	1,746	2,190	1,968
Profit discontinued operation	250	0	0	0	0
Profit for the year	1,154	1,364	1,746	2,190	1,968
Profit attributable to shareholders	1,123	1,325	1,679	2,105	1,893
Minority interest	31	40	67	84	76

Source: The company, SBI E2-Capital

Figure 9: Balance sheet

	FY12/12	FY12/13	FY12/14E	FY12/15E	FY12/16E
Non-Current Assets					
PPE	1,471	1,587	1,543	1,493	1,443
Intangible assets	614	1,096	1,325	1,289	1,253
Other receivables and deposits	2,603	3,024	4,392	5,021	3,183
Gross amounts due from customers for contract work	6,890	9,035	10,933	15,528	16,343
Other	266	484	484	484	484
Total Non-Current Assets	11,844	15,227	18,677	23,816	22,707
Current Assets					
Inventories	65	76	111	117	117
Debtors, other receivables, deposits and prepayments	1,207	1,377	1,882	2,152	1,364
Gross amounts due from customers for contract work	644	941	992	1,408	1,464
Other	1,016	1,425	1,025	1,025	1,025
Cash and cash equivalent	1,807	4,426	4,558	1,865	2,838
Total Current Assets	4,739	8,244	8,568	6,568	6,808
Total Assets	16,583	23,471	27,245	30,384	29,515
Current Liabilities					
Bank loans	1,635	1,780	1,953	2,210	1,990
Creditors, other payables and accrued expenses	1,191	1,734	2,511	2,744	1,251
Current taxation	58	58	77	96	88
Total Current Liabilities	2,884	3,572	4,540	5,050	3,328
Non-Current Liabilities					
Bank loans	4,369	5,141	6,537	7,398	6,661
Other loans	0	0	0	0	0
Deferred tax liabilities	659	979	979	979	979
Total Non Current Liabilities	5,028	6,120	7,516	8,376	7,639
Equity					
Share capital	404	448	448	448	448
Reserves	7,946	12,926	14,282	15,983	17,511
Total Shareholder's Equity	8,350	13,374	14,730	16,431	17,960
Minority interest	321	405	459	527	588
Total Equity	8,670	13,779	15,189	16,958	18,548

Source: The company, SBI E2-Capital

Figure 10: Cash flow statement

	FY12/12	FY12/13	FY12/14E	FY12/15E	FY12/16E
Operating Cash flow					
Profit before tax	1,459	1,812	2,242	2,812	2,537
Depreciation	53	49	50	50	50
Amortisation of intangible assets	29	17	17	36	36
Finance costs	315	-	467	528	519
Other	(261)	(234)	(78)	(69)	(42)
Operating Cash flow before W/C	1,594	1,643	2,698	3,357	3,100
Change in Working Capital	(1,766)	(2,500)	(3,080)	(5,684)	262
Interest received	25	-	78	69	42
Tax paid	(143)	(121)	(478)	(603)	(577)
Cash flow from operation	(290)	(978)	(783)	(2,860)	2,827
Investing Activities					
Purchases of PPE	(621)	(166)	(6)	0	0
Payment for additions of intangible assets	(103)	(499)	(245)	0	0
Other	(338)	(0)	402	0	0
Cash flow from investing activities	(1,063)	(665)	151	0	0
Financing Activities					
Proceeds from new bank loans	2,773	917	1,569	1,117	(957)
Repayment of bank loans	(1,815)	-	-	-	-
Interest paid	(315)	-	(467)	(528)	(519)
Dividend paid	(246)	(366)	(336)	(421)	(379)
Other	1,061	3,711	(3)	0	0
Cash flow from financing activities	1,458	4,262	763	168	(1,855)
Net increase in cash and cash equivalent	105	2,619	132	(2,692)	973
Cash and Cash equivalents at the Beginning of the year	1,684	1,807	4,426	4,558	1,865
Effect of foreign rate exchange	17	0	0	0	0
Cash and Cash Equivalents at the End of the year	1,807	4,426	4,558	1,865	2,838

Source: The company, SBI E2-Capital

SBI E2-Capital is a dedicated small/mid cap investment banking/ stockbrokerage house. Find our research on: sbie2capital.com, thomsononeanalytics.com, factset.com and multex.com

SBI E2-Capital stock ratings:

- STRONG BUY** : absolute upside of >50% over the next three months
- BUY** : absolute upside of >10% over the next six months
- HOLD** : absolute return of -10% to +10% over the next six months
- SELL** : absolute downside of >10% over the next six months

Investors should assume that SBI E2-Capital is seeking or will seek investment banking or other related businesses with the companies in this report.

Analyst certification: The views expressed in this report accurately reflect the analyst's personal views of the subject securities and that the analyst has not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report.

Disclaimer:

This research report is not an offer to sell or the solicitation of an offer to buy or subscribe for any securities. The securities referred to in this report may not be eligible for sale in some jurisdictions. The information contained in this report has been compiled by the Research Department of SBI E2-Capital Financial Services Limited ('SBI E2-Capital') from sources that it believes to be reliable but no representation, warranty or guarantee is made or given by SBI E2-Capital or any other person as to its accuracy or completeness. All opinions and estimates expressed in this report are (unless otherwise indicated) entirely those of SBI E2-Capital as of the date of this report only and are subject to change without notice. Neither SBI E2-Capital nor any other person, accepts any liability whatsoever for any loss howsoever arising from any use of this report or its contents or otherwise arising in connection therewith. Each recipient of this report shall be solely responsible for making its own independent investigation of the business, financial condition and prospects of the companies referred to in this report. SBI E2-Capital and their respective officers, directors and employees, including persons involved in the preparation or issuance of this report, may from time to time (1) have positions in, and buy or sell, the securities of companies referred to in this report (or related investments); (2) have a consulting, investment banking or broking relationship with any company referred to in this report; and (3) to the extent permitted under applicable law, have acted upon or used the information contained or referred to in this report including effecting transactions for their own account in an investment (or related investment) in respect of any company referred to in this report, prior to or immediately following its publication. This report may not have been distributed to all recipients at the same time. This report is issued only for the information of and may only be distributed to professional investors and dealers in securities and must not be copied, published, reproduced or redistributed (in whole or in part) by any recipient for any purpose. This report is distributed in Hong Kong by SBI E2-Capital. Any recipient of this report who requires further information regarding any securities referred to in this report should contact the relevant office of SBI E2-Capital located in such recipient's home jurisdiction.

Copyright© SBI E2-Capital Financial Services Limited. All rights reserved.