

# China / Hong Kong Company Guide

# China Everbright Intl

Version 10 | Bloomberg: 257 HK EQUITY | Reuters: 0257.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

6 Mar 2018

## BUY

Last Traded Price( 5 Mar 2018): HK\$11.88(HSI : 29,886)

Price Target 12-mth: HK\$13.50 (14% upside) (Prev HK\$13.00)

### Analyst

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### What's New

- Expect record high order backlog to underpin rising capex in FY18
- Gaining market share with climbing project wins
- Targets to become a global player in the long run
- Maintain BUY with TP of HK\$13.50

### Price Relative



### Forecasts and Valuation

FY Dec (HK\$m)	2016A	2017A	2018F	2019F
Turnover	13,971	20,043	26,592	32,496
EBITDA	5,005	6,817	8,691	10,342
Pre-tax Profit	4,099	5,428	6,980	8,399
Net Profit	2,785	3,510	4,552	5,499
Net Pft (Pre Ex) (core profit)	2,785	3,510	4,552	5,499
Net Profit Gth (Pre-ex) (%)	33.6	26.0	29.7	20.8
EPS (HK\$)	0.62	0.78	1.02	1.23
Core EPS (HK\$)	0.62	0.78	1.02	1.23
EPS Gth (%)	33.6	26.0	29.7	20.8
Diluted EPS (HK\$)	0.62	0.78	1.02	1.23
DPS (HK\$)	0.21	0.24	0.41	0.49
BV Per Share (HK\$)	3.88	5.03	5.75	6.54
PE (X)	19.1	15.2	11.7	9.7
P/Cash Flow (X)	241.4	nm	nm	nm
P/Free CF (X)	nm	nm	nm	nm
EV/EBITDA (X)	14.2	12.1	10.7	10.4
Net Div Yield (%)	1.7	2.0	3.4	4.1
P/Book Value (X)	3.1	2.4	2.1	1.8
Net Debt/Equity (X)	0.8	0.8	1.0	1.3
ROAE (%)	16.0	17.6	18.8	20.0
Earnings Rev (%)			4	4
Consensus EPS (HK\$)			0.99	1.15
Other Broker Recs:		B: 25	S: 0	H: 2

Source of all data on this page: Company, DBSV, Thomson Reuters, HKEX

## Growing even bigger

**Higher earnings on rising capex.** We maintain our BUY rating on China Everbright International (CEI). We expect earnings to continue to grow along with higher project wins and capex in FY18. Its strong R&D in technology allows it to increase market share, extend its business scope and expand into overseas markets to become a global player.

**We are at the high-end of consensus range.** We reckon the market is too conservative on CEI's turnover growth. CEI's deal flow remains very solid with order backlog climbing 35% to historical high. We are optimistic that capex will also increase 30%, leading to strong growth of 31% in construction revenue. There should be further room to raise consensus estimates on both top- and bottom-line. Our FY19 projections for turnover and net profit are 19% and 7% higher than the market respectively.

**Growing within and outside China.** CEI's share price surged as much as 15% in the past four weeks and we see possibility of short term profit taking after the results. However, any project wins in overseas markets paves the way for CEI to become a global player. More new deals within China and strong earnings delivery are catalysts.

### Valuation:

We have fine-tuned our earnings estimates and our TP is raised from HK\$13.00 to HK\$13.50 which is based on the target valuation of China Everbright Water (CEWL SP, \$0.65 TP), 23x and 18x 12-month rolling adjusted PE for waste-to-energy and greentech operations respectively, with earnings from construction revenue excluded.

### Key Risks to Our View:

Slower-than-expected construction progress, fewer-than-expected project wins and reduction in feed-in-tariffs will lead to lower earnings growth.

### At A Glance

Issued Capital (m shrs)	4,483
Mkt. Cap (HK\$m/US\$m)	53,255 / 6,800
Major Shareholders	
China Everbright Hldgs (%)	41.4
RRJ Capital Master Fund II, L.P. (%)	7.9
Free Float (%)	50.8
3m Avg. Daily Val. (US\$m)	15.2
ICB Industry: Industrials / Support Services	

**WHAT'S NEW****Expect project wins and capex to continue to climb****Expanded business scale with broadened service scope.**

During the results briefing, Mr. Wang Tianyi, the new CEO, shared the company's development targets of becoming the leading enterprise in the environmental protection industry in China and a world-renowned environmental protection company. These will be achieved through expansion in both operation scale and service scope. Apart from soil remediation, CEI is looking into extending along the value chain in waste-to-energy, such as environmental sanitation or waste segregation. He quantified the target only for China Everbright Water (CEWL SP) where capacity will double by 2020, but not for the WTE operation and China Everbright Greentech (1257 HK). Nevertheless, we expect CEI to ride on the current investment wave in environmental protection which is one of the government's main focus areas. We expect project wins in FY18 to be at least the amount clinched in FY17, i.e. Rmb20bn.

**Expand overseas.** In addition, CEI targets to become a leading player in the global environmental protection industry in 5-10 years. Currently, CEI's international exposure is very limited with a waste treatment company in Poland, a WTE project in Vietnam and a ground photovoltaic project in Germany.

While there are many opportunities available in overseas markets, CEI has been very selective and carefully assesses the risk and return. It is also flexible in terms of the business model, including export of equipment, entrusted operations or project investment.

**Higher capex in FY18.** Although management did not specify any short term targets, we are optimistic that CEI will have a higher capex of HK\$13bn in FY18, compared with c.HK\$10bn in FY17. This is underpinned by its record high order backlog of Rmb36.4bn, compared with Rmb27bn at the end of FY17. As at the end of FY17, 39 projects with a total investment of Rmb19bn were still under construction. Thus, we raised our growth assumption for construction revenue by 7ppts to 31% in FY18.

**Rising operating capacity.** Upon the completion of construction of 45 projects with a total investment of Rmb11.5bn in FY17, these projects will turn into operating capacity. Thus, we raised total operating revenue by 16% in FY18.

**Income Statement (HK\$ m)**

FY Dec	2016A	2017A	% chg yoy
Revenue	13,971	20,043	43.5
Cost of Goods Sold	(8,662)	(12,911)	49.1
<b>Gross Profit</b>	<b>5,310</b>	<b>7,133</b>	<b>34.3</b>
Other Opng (Exp)/Inc	(681)	(873)	28.2
<b>Operating Profit</b>	<b>4,629</b>	<b>6,260</b>	<b>35.2</b>
Other Non Opg (Exp)/Inc	0	0	nm
Associates & JV Inc	63	60	(4.3)
Net Interest (Exp)/Inc	(593)	(892)	(50.4)
Exceptional Gain/(Loss)	0	0	nm
<b>Pre-tax Profit</b>	<b>4,099</b>	<b>5,428</b>	<b>32.4</b>
Tax	(1,062)	(1,376)	29.6
Minority Interest	(252)	(542)	(115.3)
<b>Net Profit</b>	<b>2,785</b>	<b>3,510</b>	<b>26.0</b>
Net Profit before Except.	2,785	3,510	26.0
EBITDA	5,005	6,817	36.2
<b>Margins &amp; Ratio</b>			
Gross Margins (%)	38.0	35.6	
Opg Profit Margin (%)	33.1	31.2	
Net Profit Margin (%)	19.9	17.5	

Source: Company, DBS Vickers

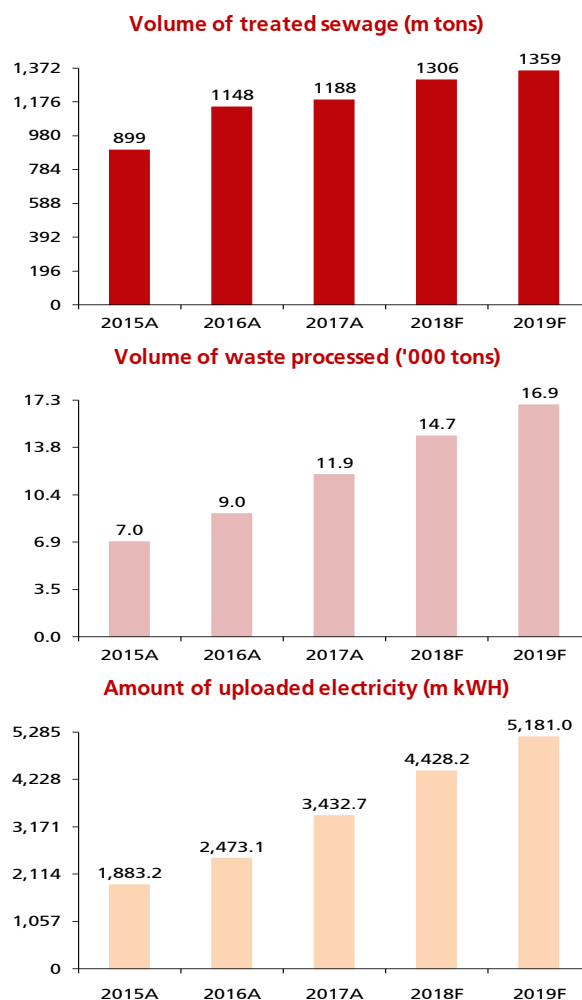
## CRITICAL FACTORS TO WATCH

### Critical Factors

**Rising project wins, order backlog and capex.** CEI secured 54 new project wins and signed 3 supplementary agreements for project expansion, with total investment of c.Rmb20bn in FY17, compared with project wins of Rmb14bn in FY16. We are optimistic that CEI's new project wins in FY18 will be at a record high. These new projects have lifted the order backlog to a new peak of Rmb36.4bn as at Dec 2017, up from Rmb27bn in Dec 2016. We estimate FY18 capex to be HK\$13bn, up from HK\$10bn in FY17. Strong spending in projects will underpin robust growth in construction revenue in the coming 12-24 months.

**Set up of Envirotech to strengthen competitiveness.** After several acquisitions (including Jiangsu Design & Research Institute and Nanjing Science and Technology Building) and establishing an Environmental Energy Center with Zhejiang University, CEI has put together all its R&D capabilities to set up an Envirotech division. Through this new technology platform, CEI covers the entire waste-to-energy (WTE) value chain and has also imported new technologies and materials. Not only can CEI strengthen its cost advantages, this also helps CEI to explore more business opportunities. For instance, CEI clinched its first project in river restoration and urban-rural integration water supply as well as underground waste water treatment projects. CEI is now making solid progress in more new areas, such as 850 tons/day grate furnace, reciprocating water-cooled biomass grate furnace, plasma melting system for hazardous waste treatment, etc. We reckon these breakthroughs allow CEI to win more projects through the provision of more bundling services in both China and overseas, including environmental services and equipment.

**Market competition.** Although market competition is still keen, it has subsided slightly from before with project returns sustaining at a reasonable level. Despite this, CEI maintains a minimum IRR requirement of 8% for water projects and 10% for WTE and Greentech projects. It also takes steps to continuously strengthen its competitive edge to maintain its leading position in the market.

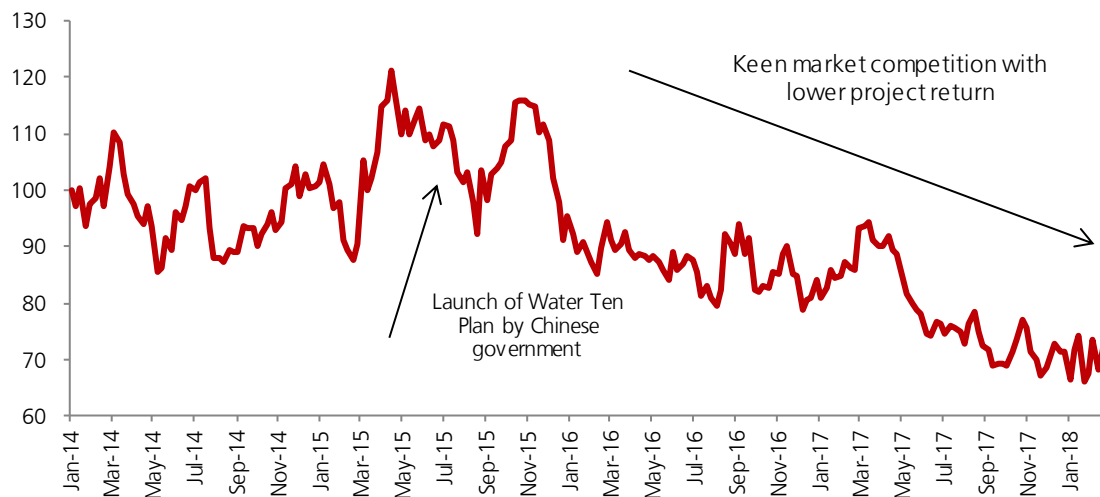


Source: Company, DBS Vickers

**Appendix 1: A look at Company's listed history – what drives its share price?**

**Share price performance vs HSI**

CEI rel to HSI (Rebased Jan 14 = 100)



Source: Thomson Reuters, DBS Vickers

### Balance Sheet:

**Healthy gearing ratio.** Following its high cash outflow for construction of projects, CEI's net debt-equity ratio climbed to 80% at Dec 2017. We estimate the ratio will climb further to 100% in Dec 2018 as more capex is put into projects.

### Share Price Drivers:

**Strong deal flow.** Stronger than expected deal flow will provide upside to earnings growth and share price.

**Market competition.** Fierce market competition will put pressure on project returns and earnings.

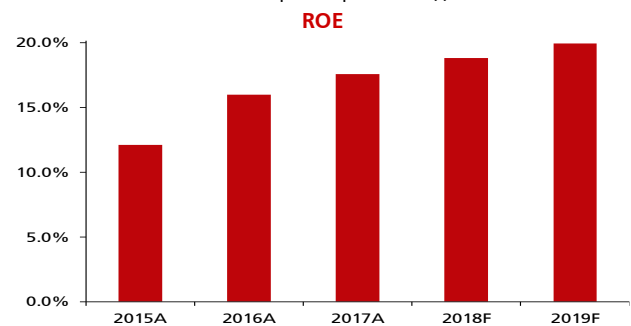
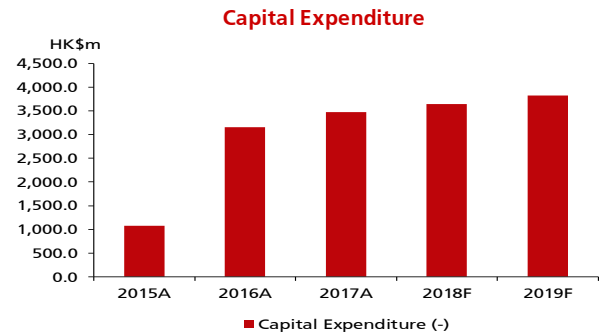
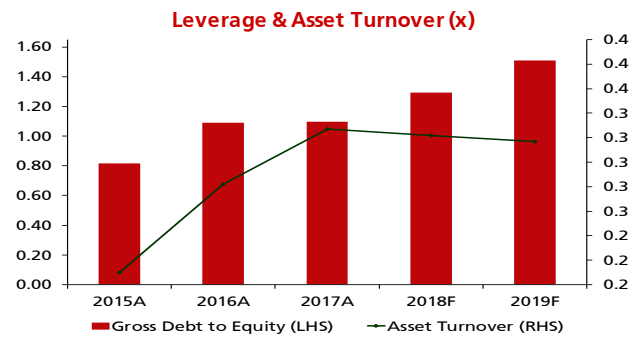
### Key Risks:

**Project win and construction progress.** Slower-than-expected progress in construction, fewer-than-expected project wins and reduction of feed-in tariff will lead to lower earnings growth.

**Interest rate hike.** The U.S. central bank would likely continue with gradual rate hikes despite uncertainty about inflation. Monetary tightening in China is also expected to continue in 2018. These will raise average funding cost for CEI. In an interest rate hike cycle, investors' appetite for high debt level companies would also decline.

### Company Background

China Everbright International is a comprehensive environmental service provider in China. Its services include waste water treatment, waste-to-energy, photovoltaic and biomass power generation.



Source: Company, DBS Vickers

**Key Assumptions**

FY Dec	2015A	2016A	2017A	2018F	2019F
Volume of treated sewage (m tons)	899.2	1,148.3	1,187.6	1,306.4	1,358.6
Volume of waste processed ('000 tons)	7.0	9.0	11.9	14.7	16.9
Amount of uploaded electricity (m kWH)	1,883.2	2,473.1	3,432.7	4,428.2	5,181.0

Source: Company, DBS Vickers

**Segmental Breakdown (HK\$ m)**

FY Dec	2015A	2016A	2017A	2018F	2019F
<b>Revenues (HK\$ m)</b>					
Environmental Energy	5,401	7,784	11,060	15,008	18,262
Environmental Water	1,815	2,494	3,592	4,401	5,091
Greentech	1,178	3,026	4,580	6,250	8,070
Others	135	667	812	933	1,073
<b>Total</b>	<b>8,528</b>	<b>13,971</b>	<b>20,043</b>	<b>26,592</b>	<b>32,496</b>

**Segmental profit (HK\$ m)**

Environmental Energy	2,670	3,270	4,191	4,378	5,177
Environmental Water	796	844	1,187	1,187	1,400
Greentech	437	1,020	1,543	1,607	2,168
Others	171	417	536	915	1,055
<b>Total</b>	<b>4,073</b>	<b>5,551</b>	<b>7,457</b>	<b>8,086</b>	<b>9,801</b>

**Segmental profit Margins (%)**

Environmental Energy	49.4	42.0	37.9	29.2	28.4
Environmental Water	43.9	33.8	33.1	27.0	27.5
Greentech	37.1	33.7	33.7	25.7	26.9
Others	126.4	62.5	66.0	98.0	98.3
<b>Total</b>	<b>47.8</b>	<b>39.7</b>	<b>37.2</b>	<b>30.4</b>	<b>30.2</b>

Source: Company, DBS Vickers

### Income Statement (HK\$ m)

FY Dec	2015A	2016A	2017A	2018F	2019F
Revenue	8,528	13,971	20,043	26,592	32,496
Cost of Goods Sold	(4,626)	(8,662)	(12,911)	(16,922)	(20,878)
<b>Gross Profit</b>	<b>3,903</b>	<b>5,310</b>	<b>7,133</b>	<b>9,670</b>	<b>11,618</b>
Other Opng (Exp)/Inc	(378)	(681)	(873)	(1,575)	(1,917)
<b>Operating Profit</b>	<b>3,524</b>	<b>4,629</b>	<b>6,260</b>	<b>8,095</b>	<b>9,702</b>
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	(6)	63	60	66	73
Net Interest (Exp)/Inc	(400)	(593)	(892)	(1,181)	(1,375)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>3,119</b>	<b>4,099</b>	<b>5,428</b>	<b>6,980</b>	<b>8,399</b>
Tax	(783)	(1,062)	(1,376)	(1,815)	(2,184)
Minority Interest	(251)	(252)	(542)	(614)	(716)
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>2,085</b>	<b>2,785</b>	<b>3,510</b>	<b>4,552</b>	<b>5,499</b>
Net Profit before Except.	2,085	2,785	3,510	4,552	5,499
EBITDA	3,702	5,005	6,817	8,691	10,342
<b>Growth</b>					
Revenue Gth (%)	34.2	63.8	43.5	32.7	22.2
EBITDA Gth (%)	35.5	35.2	36.2	27.5	19.0
Opg Profit Gth (%)	34.6	31.3	35.2	29.3	19.8
Net Profit Gth (%)	22.4	33.6	26.0	29.7	20.8
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	45.8	38.0	35.6	36.4	35.8
Opg Profit Margin (%)	41.3	33.1	31.2	30.4	29.9
Net Profit Margin (%)	24.4	19.9	17.5	17.1	16.9
ROAE (%)	12.1	16.0	17.6	18.8	20.0
ROA (%)	5.1	5.6	5.7	5.5	5.4
ROCE (%)	7.0	7.7	8.6	8.4	8.2
Div Payout Ratio (%)	39.8	33.0	30.7	40.0	40.0
Net Interest Cover (x)	8.8	7.8	7.0	6.9	7.1

Source: Company, DBS Vickers

### Interim Income Statement (HK\$ m)

FY Dec	2H2015	1H2016	2H2016	1H2017	2H2017
Revenue	4,765	5,421	8,551	9,142	10,901
Cost of Goods Sold	(2,654)	(3,168)	(5,494)	(5,835)	(7,076)
<b>Gross Profit</b>	<b>2,111</b>	<b>2,253</b>	<b>3,057</b>	<b>3,308</b>	<b>3,825</b>
Other Oper. (Exp)/Inc	(229)	(208)	(347)	(302)	(524)
<b>Operating Profit</b>	<b>1,883</b>	<b>2,045</b>	<b>2,710</b>	<b>3,006</b>	<b>3,301</b>
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	(6)	24	39	28	33
Net Interest (Exp)/Inc	(228)	(300)	(339)	(411)	(528)
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>1,649</b>	<b>1,769</b>	<b>2,410</b>	<b>2,623</b>	<b>2,805</b>
Tax	(417)	(471)	(592)	(624)	(752)
Minority Interest	(148)	(89)	(163)	(203)	(339)
<b>Net Profit</b>	<b>1,085</b>	<b>1,209</b>	<b>1,655</b>	<b>1,796</b>	<b>1,714</b>
Net profit bef Except.	1,085	1,209	1,655	1,796	1,714
<b>Growth</b>					
Revenue Gth (%)	39.7	43.8	79.4	68.7	27.5
Opg Profit Gth (%)	31.6	20.7	44.0	47.0	21.8
Net Profit Gth (%)	20.4	20.9	52.6	48.5	3.5
<b>Margins</b>					
Gross Margins (%)	44.3	41.6	35.7	36.2	35.1
Opg Profit Margins (%)	39.5	37.7	31.7	32.9	30.3
Net Profit Margins (%)	22.8	22.3	19.4	19.6	15.7

Source: Company, DBS Vickers

## Balance Sheet (HK\$ m)

FY Dec	2015A	2016A	2017A	2018F	2019F
Net Fixed Assets	2,667	3,339	4,361	7,755	11,294
Invt in Associates & JVs	449	573	792	858	931
Other LT Assets	26,019	33,313	48,333	62,680	79,975
Cash & ST Invt	5,954	6,341	8,657	9,307	8,124
Inventory	202	362	510	532	650
Debtors	4,612	4,908	8,289	9,533	9,916
Other Current Assets	720	697	2,181	1,596	1,950
<b>Total Assets</b>	<b>40,623</b>	<b>49,532</b>	<b>73,123</b>	<b>92,262</b>	<b>112,839</b>
ST Debt	3,410	4,412	5,414	6,014	6,514
Creditors	2,838	4,898	8,599	13,271	16,217
Other Current Liab	119	98	114	114	114
LT Debt	12,411	17,204	26,040	36,053	48,942
Other LT Liabilities	2,425	3,076	4,312	4,312	4,312
Shareholder's Equity	17,196	17,389	22,554	25,795	29,322
Minority Interests	2,224	2,456	6,089	6,703	7,419
<b>Total Cap. &amp; Liab.</b>	<b>40,623</b>	<b>49,532</b>	<b>73,123</b>	<b>92,262</b>	<b>112,839</b>
Non-Cash Wkg. Capital	2,577	971	2,267	(1,724)	(3,816)
Net Cash/(Debt)	(9,867)	(15,275)	(22,797)	(32,760)	(47,331)
Debtors Turn (avg days)	197.4	128.2	120.2	122.3	109.2
Creditors Turn (avg days)	233.2	214.1	198.4	243.5	265.0
Inventory Turn (avg days)	16.6	15.8	12.8	11.6	10.6
Asset Turnover (x)	0.2	0.3	0.3	0.3	0.3
Current Ratio (x)	1.8	1.3	1.4	1.1	0.9
Quick Ratio (x)	1.7	1.2	1.2	1.0	0.8
Net Debt/Equity (X)	0.5	0.8	0.8	1.0	1.3
Net Debt/Equity ex MI (X)	0.6	0.9	1.0	1.3	1.6
Capex to Debt (%)	6.8	14.6	11.0	8.7	6.9
Z-Score (X)	2.3	1.9	1.7	1.7	1.5

Source: Company, DBS Vickers

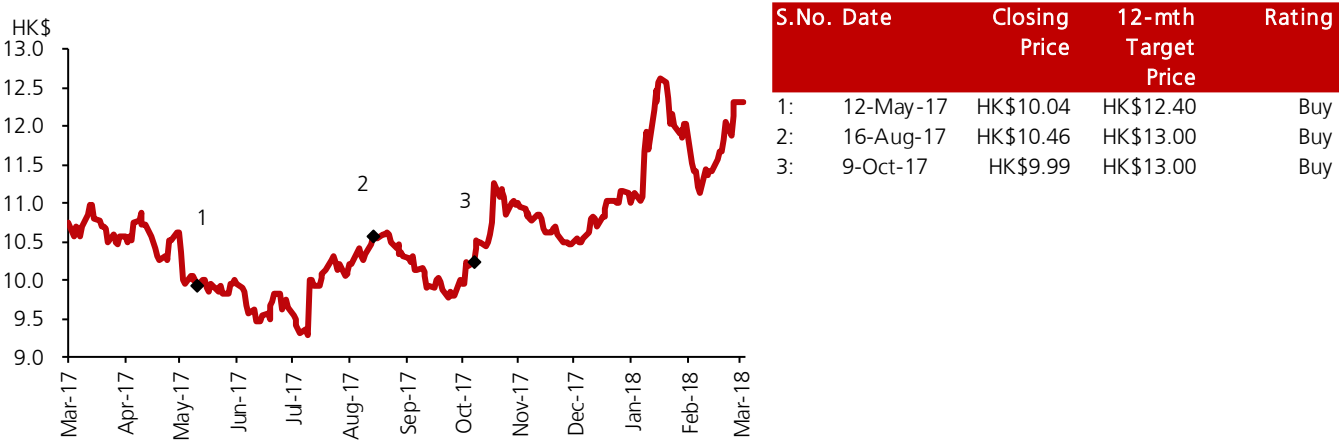


Cash Flow Statement (HK\$ m)

FY Dec	2015A	2016A	2017A	2018F	2019F
Pre-Tax Profit	3,119	4,099	5,428	6,980	8,399
Dep. & Amort.	184	313	497	530	567
Tax Paid	(217)	(335)	(436)	(1,815)	(2,184)
Assoc. & JV Inc/(loss)	6	(63)	(60)	(66)	(73)
(Pft)/ Loss on disposal of FAs	1	11	0	0	0
Chg in Wkg.Cap.	(4,839)	(4,330)	(6,729)	(9,134)	(13,981)
Other Operating CF	208	525	(200)	1,181	1,375
<b>Net Operating CF</b>	<b>(1,538)</b>	<b>221</b>	<b>(1,500)</b>	<b>(2,325)</b>	<b>(5,896)</b>
Capital Exp.(net)	(1,082)	(3,157)	(3,472)	(3,646)	(3,828)
Other Invts.(net)	0	0	0	0	0
Invts in Assoc. & JV	(186)	(98)	(218)	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(1,408)	(981)	0	(1,500)	(1,500)
<b>Net Investing CF</b>	<b>(2,676)</b>	<b>(4,236)</b>	<b>(3,690)</b>	<b>(5,146)</b>	<b>(5,328)</b>
Div Paid	(560)	(906)	(1,076)	(1,311)	(1,972)
Chg in Gross Debt	6,793	6,220	9,838	10,613	13,388
Capital Issues	0	(8)	0	0	0
Other Financing CF	(29)	(592)	(1,255)	(1,181)	N/A
<b>Net Financing CF</b>	<b>6,204</b>	<b>4,713</b>	<b>7,507</b>	<b>8,121</b>	<b>10,041</b>
Currency Adjustments	(130)	(311)	0	0	0
Chg in Cash	1,859	387	2,317	650	(1,183)
Opg CFPS (HK\$)	0.74	1.02	1.17	1.52	1.80
Free CFPS (HK\$)	(0.58)	(0.65)	(1.11)	(1.33)	(2.17)

Source: Company, DBS Vickers

Target Price & Ratings History



Source: DBS Vickers

Analyst: Patricia YEUNG

DBSVHK recommendations are based on Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

**HOLD** (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

**FULLY VALUED** (negative total return i.e. > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

*Share price appreciation + dividends*

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Sources for all charts and tables are DBS Vickers unless otherwise specified.

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