

Canvest Environmental Protection Group Co., Ltd. (1381.HK)

Exceptional Results with Enormous Market Potential

20 JULY 2016

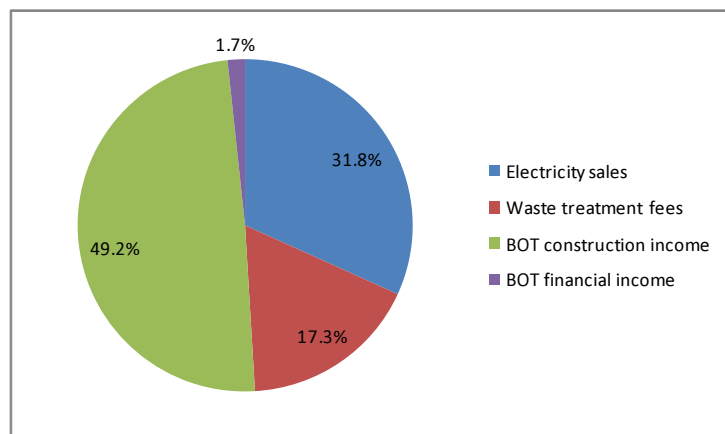
Hong Kong | Public Utility | Company report

Rapid Growth in Operating Results

Canvest Environmental Protection Group Company Limited is a leading pure waste-to-energy (WTE) provider focused solely on the development, management and operation of WTE plants. In 2015, the revenue of Canvest amounted to HK\$1.19 billion, representing a year-on-year increase of 49.2%, which was mainly attributable to the following two factors: i) The revenue derived from BOT construction of Zhanjiang WTE plants skyrocketed by 135.4%, reaching HK\$580 million and accounting for 49.2% of the total revenue; ii) The efficient operations of two WTE projects Kewei and China Scivest. During the reporting period, the company processed a total of 1.5 million tones of harmless waste and achieved a total power generation of 660 million kwh.

The company's gross profit was HK\$440 million, an increase of 28.3% year-on-year. Its gross profit margin dropped from 43.1% in 2014 to 37.1% in 2015, mainly because the gross profit margin of the BOT construction business (16.7%) was far lower than that of WTE electricity sales and waste processing (55.4%). During the reporting period, the company's financial expenses declined by 16.8%. Besides, net profit attributable to parent company amounted to HK\$270 million, surging by 42.4% year-on-year. Basic EPS was HK\$13.6 cents.

Company's revenue by division in 2015



Source: Company's 2015 annual report

Buy (Maintain)

CMP: HKD 3.40

(Closing price as at 18 July 2016)

TARGET: 4.70 (+38%)

COMPANY DATA

O/S SHARES (MN) :	2034
MARKET CAP (HKDMN) :	6916
52 - WK HI/LO (HKD):	4.06/2.74

SHARE HOLDING PATTERN, %

Zhenda Development Co, Ltd. :	64.00
AEP Green Power, Ltd	6.31

PRICE PERFORMANCE, %

	1M	3M	1Y
Canvest Environmental Protection	-6.08	-7.61	-12.60
HSI	8.10	3.03	-14.21

KEY FINANCIALS

CNY mn	FY14	FY15	FY16F	FY17F
Net Sales	794	1185	1583	2141
Net Profit	191	272	400	530
EPS, HKD	0.13	0.14	0.20	0.26
PER, x	26.8	25.0	17.3	13.1
BVPS, HKD	1.16	1.17	1.36	1.62
P/BV, x	2.9	2.9	2.5	2.1
ROE, %	12.8	11.7	15.8	17.7
Debt/Equity,%	55.8	91.4	92.3	100.0

Source: Company reports, Phillip Securities Est.

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Abundant Project Reserve

The company now is present on the market in Guangdong Province, Guangxi Zhuang Autonomous Region and Guizhou Province. As at the end of 2015, the daily municipal domestic waste (MSW) processing capacity of the company's operations, together with the daily MSW processing capacity of the secured contracts, increased by approximately 80% to 12,400 tonnes on a year-on-year basis. The processing capacity of operations soared from 3,600 tonnes to 5,400 tonnes, up by 50%. In 2016, the company accelerated the pace of expansion. It successfully acquired the approved expansion of China Scivest and the acquisition of Xingyi project and obtained the BOT concession right of Beiliu WTE plant, which will further increase the total capacity to 15,700 tonnes. Rapid expansion of reserved projects will give a definite opportunity for growth in the future. Echo-Tech phase I, after technological upgrade this year, will be put into operation. In addition, Zhanjiang project began to be put into operation in Q2, making the total projects capacity surge to 7,600 tonnes per day, much larger than 2015. The company is therefore expected to record a large increase in operating result in 2016. Besides, given the increasingly intense competition in the industry over the past two years, some companies secured projects by means of lowering the waste processing fee. But the company indicated that it would not greatly cut the waste processing fee in order to acquire a certain project. The waste processing fee of projects obtained in the past 15 months was high. In some underdeveloped areas, if the price was too low, the company would not participate in the bidding.

Huge Market Potential of Technological Upgrade

In 2014, about 25% of domestic WTE plants adopted fluidized bed technology. However, since the moving grate technology is more environmentally friendly and causes fewer pollution problems, the existing WTE plants that run on the fluidized bed technology will have to undergo technological upgrade of moving grate technology. Canvest has an edge over other WTE enterprises in terms of technological upgrade market. The company has rich experience in upgrading circulating fluidized bed to moving grate with Eco-Tech and China Scivest subject to major technological upgrade. Therefore, the company has accumulated abundant experience in technological upgrade. After the upgrade, the projects of Eco-Tech and China Scivest reached an exceedingly high level of operation. The auxiliary power consumption rate is as low as 12%, well below the industry average level of 15% -18%. In this way, economic efficiency is not only greatly enhanced, but better environmental benefits are created as well. In addition, the company also plans to undertake technological upgrade of Guangxi Laibin and Guizhou Xingyi projects in order to improve its overall performance.

Evaluation

The WTE market in Guangdong Province is growing rapidly, and the compound annual growth rate of its daily processing capacity from 2015 to 2020 is anticipated to reach 18%.

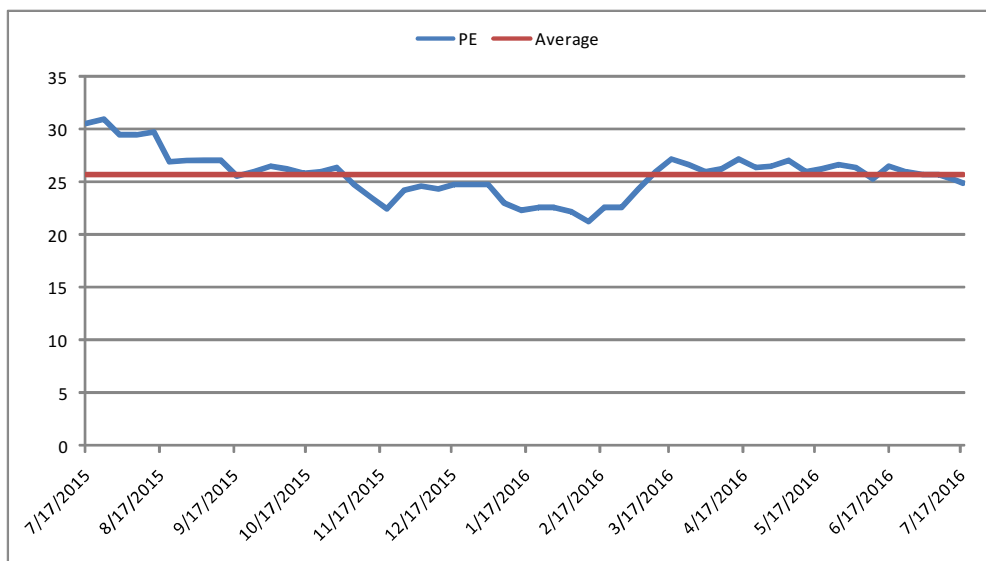
Canvest is equipped with rich experience and advantages of mature technological upgrade in respect of project implementation, so it is expected that the company will benefit from the fast-growing market of Guangdong Province. We give the company the target price of HK\$4.7, equivalent to 18X P/E in 2017. The "Buy" rating is maintained. (Closing price as at 18 July 2016)

P/E Comparison of peer companies

Company	Code	PE x
China Everbright Intl Ltd	257 HK	17.74
Dynagreen Environmental Protection	1330 HK	13.45
Canvest Environmental Protection	1381 HK	25
Average		18.73

Source: Bloomberg, Phillip Securities (HK) Research

Historical P/E Valuation



Source: Bloomberg, Phillip Securities (HK) Research

Risk warnings

New projects fell short of expectation;

RMB devaluation.

Financials

FYE	2013	2014	2015	2016F	2017F
Valuation Ratios					
Price Earnings	NA	26.8x	25.0x	17.3x	13.1x
Price to Book	NA	2.9x	2.9x	2.5x	2.1x
Dividend Yield	NA	0.0%	0.0%	0.0%	0.0%
Per share data(HKD)					
EPS Adjusted	NA	0.13	0.14	0.20	0.26
Book Value Per Share	NA	1.16	1.17	1.36	1.62
Dividends Per Share	NA	0.00	0.00	0.00	0.00
Growth & Margin					
Revenue growth	0.8%	103.5%	49.2%	33.7%	35.2%
Gross Profit growth	-2.0%	68.9%	28.3%	33.6%	26.1%
Net Profit growth	3.5%	45.9%	42.4%	47.0%	32.4%
Profitability Ratios					
Gross Margin	51.9%	43.1%	37.1%	37.1%	34.6%
Net Profit Margin	33.6%	26.2%	24.4%	26.3%	25.5%
Dividend Payout Ratio %	NA	0.0%	0.0%	0.0%	0.0%
Key Ratios					
Return on Assets	11.7%	7.6%	6.6%	8.2%	9.0%
Return on Equity	28.9%	12.8%	11.7%	15.8%	17.7%
Effective Tax Rate	11.7%	11.6%	12.4%	12.0%	12.0%
Liability ratio	38.6%	35.8%	47.8%	48.0%	50.0%
Income Statement(HKD: mn)					
Revenue	390	794	1,185	1,583	2,141
- Cost of Goods Sold	188	452	745	996	1,401
Gross Income	203	342	439	587	740
- Selling, General & Admin Expenses	42	107	112	158	214
Operating Income	175	294	377	529	676
- Interest Expense	27	67	63	65	65
- Net Non-Operating Losses (Gains)	-1	-6	-12	-10	-10
Pretax Income	148	236	330	474	621
- Income Tax Expense	17	27	41	57	75
Income Before XO Items	131	208	289	417	546
- Minority Interests	0	17	17	17	17
Net Profit	131	191	272	400	530

Source: Company, Phillip Securities (HK) Research Estimates
(Financial figures as at 7 June 2016)

PHILLIP RESEARCH STOCK SELECTION SYSTEMS

Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within $\pm 5\%$ from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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