

# China Resources Power (836.HK)

## Stable earnings, low valuations

Hong Kong | Electricity Supply | Company Report

23 March 2017

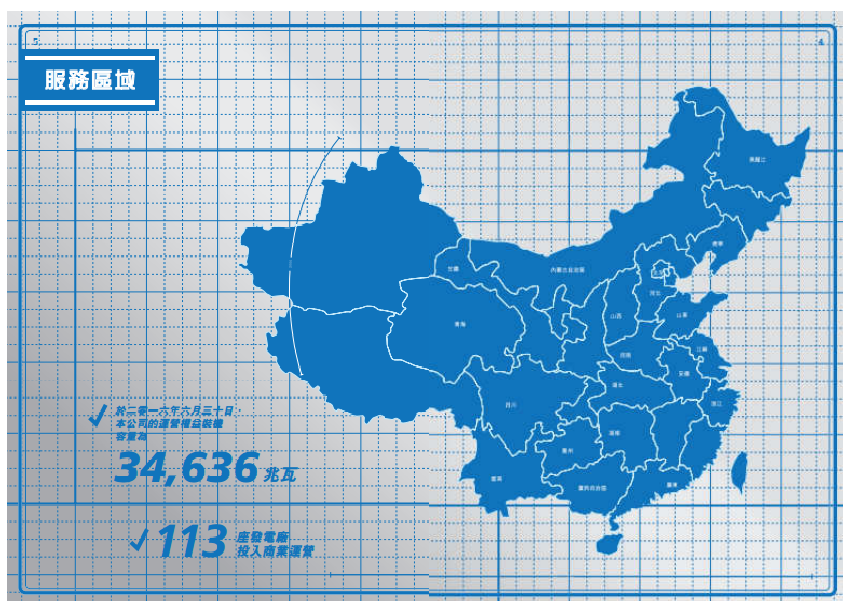
### Investment Summary

- Coal-power keep weakening earning power. However, the valuation is attractive.
- Bottomed power consumption in China, and coal-fired power capacity cut could be beneficial to the group's long-term earning power.
- China coal price correction possibly continue, beneficial to the group's cost controlling.

### Company Overview

China Resources Power Holdings Company Limited mainly engaged in in the development, construction and operation of power plants, including large-scale efficient coal-fired generation units and various clean and renewable energy projects as well as development, construction and operation of coal mines. According to the 1H2016 interim result, CR Power has 38 coal-fired power plants, 2 hydro-electric plants, 1 gasfired plant, 67 wind farms and 5 photovoltaic power plants in commercial operation. The total attributable operational generation capacity of the Company is 34,636MW, coal-fired power plants accounted for 85.9% or 29,746MW, while those of wind power, hydropower, photovoltaic power and gas-fired power together accounted for 14.1%, representing an increase of 0.8 percentage point over 13.3% as at the end of 2015. With 5.9% of our capacity located in Eastern China, 27.3% located in Central China, 19.3% located in Southern China, 10.7% located in Northern China, 5.0% located in Northeastern China, 1.1% located in Southwestern China and 0.7% located in Northwestern China.

Below is a diagram to show the distribution of power plants of the company:



Source: Company reports, Phillip Securities (HK) Research

### Accumulate

CMP: HKD 15.04  
(Closing price as at 21 MAR 2017)  
TARGET: HKD 16.72 (+11.17%)

#### COMPANY DATA

O/S SHARES (MN) :	4,808
MARKET CAP (HKDMN) :	71,743
52 - WK HI/LO (HKD):	10.70/ 15.50

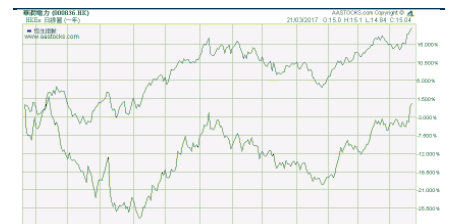
#### SHARE HOLDING PATTERN, %

China Resources Holdings	62.99
--------------------------	-------

#### PRICE PERFORMANCE, %

		1M	3M	1Y
China Res Power		+4.78	+21.50	-0.40
HSI		+2.27	+12.50	+18.42

#### PRICE VS. HSI



Source: Phillip Securities (HK) Research

#### KEY FINANCIALS

HKD mn	FY14	FY15	FY16E	FY17E
EPS, HKD	1.94	2.10	1.90	1.52
PE, x	10.31	7.18	7.98	10.12
BVPS, HKD	14.76	14.75	15.85	16.27
P/BV, x	1.36	1.02	0.94	0.92
ROE, %	22.24	18.83	9.16	6.22
Debt/Equity (%)	117.07	105.71	-	-

Source: Company reports, Phillip Securities Est.

Research Analyst  
**Tim Wong**  
(+ 852 22776516)  
timwong@phillip.com.hk

According to the 1H2016 interim result, revenue of the group amounted to approximately HKD30,971 million, representing a decrease of approximately 16.2% YoY. The net profit of the company amounted to approximately HKD 5,336 million, representing a decrease of approximately 21.7% YoY. The net asset value per share amounted to approximately HKD14.73, which indicated that the stock currently trades at around its book value.

Not only the 2016 first half result was unfavorable, we are also not optimistic about the 2016 full year result. Along with overall unfavorable business environment of the power generation industry, the firm experienced tough times in last year. The most obvious problem is that, the price surge of the thermal coal resulted a significant impact on the cost of coal-power generation. Moreover, the Excess Capacity of the power generation industry is another crucial problem. China's industrial power use growth has slowed in resulting the decrease in the power industry's earnings. The group also announced that total net generation of subsidiary power plants for 2016 increased by 6.1% to 151,589,740MWh compared to 142,906,824MWh for 2015. On a same plant basis, total net generation of subsidiary coal-fired power plants in 2016 increased by 0.3% compared to 2015. The stock is trading at approximate 7.89x FY2016Est PE and 0.94x FY2016Est Price to Book Ratio, we believe most unfavorable information possibly priced in on the stock price. In last year, the stock had underperformed by around 18.86% compared with the Hang Seng Index, which the valuation might be appealing.

As the firm is one of the largest power generators in China, hard to ignore that the group is a monopoly firm, and also since the national standards for energy saving environmental protection is pushed higher and the environmental protection restrictions for energy development is much more tightened, the barriers to entry has become higher and higher for new entrants. Moreover, according to the annual meeting of parliament, the National Development and Reform Commission (NDRC) said it would shut or stop construction of coal-fired power plants with capacity of more than 50 million kilowatts. It will further consolidate the monopoly power of the group. Thereby, the group still has favorable long-term prospects.

## Peer Comparison

Ticker	P/E	P/B	Dvd Yld(%)	ROE(%)
836 HK	7.89	0.94	5.45	12.19
2380 HK	7.48	0.73	5.71	9.97
902 HK	8.45	0.91	5.98	10.64
991 HK	-	0.68	-	-3.23
1071 HK	8.63	0.69	5.15	9.16
6 HK	19.07	1.16	3.99	6.09
2 HK	15.94	2.07	3.49	13.3

Source: Bloomberg, Phillip Securities (HK) Research

The table in above shows the peer comparison of the group.

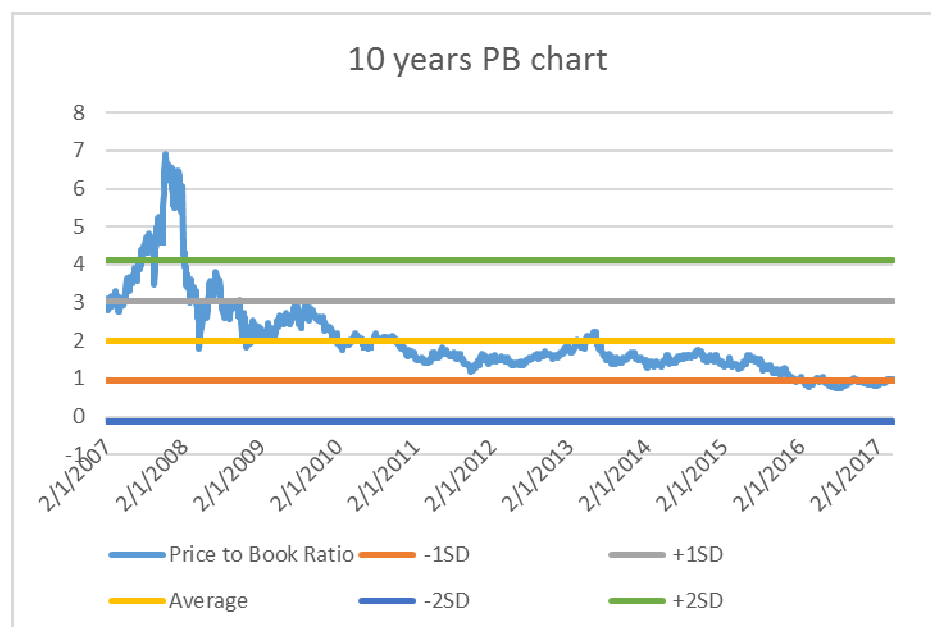
In term of PE and PB, the group is less expensive than its international peers such as Power Asset Holdings (6 HK) and CLP Holdings (2HK).

However, the valuation is slightly more expensive than its Chinese peers such as Huaneng Power (902 HK), China Power (2380 HK), and Huadian Power (1071 HK).

In term of PE, the group is slightly more expensive than Huaneng Power, and China Power. On the other hand, in term of PB, the group is more expensive than its Chinese peers.

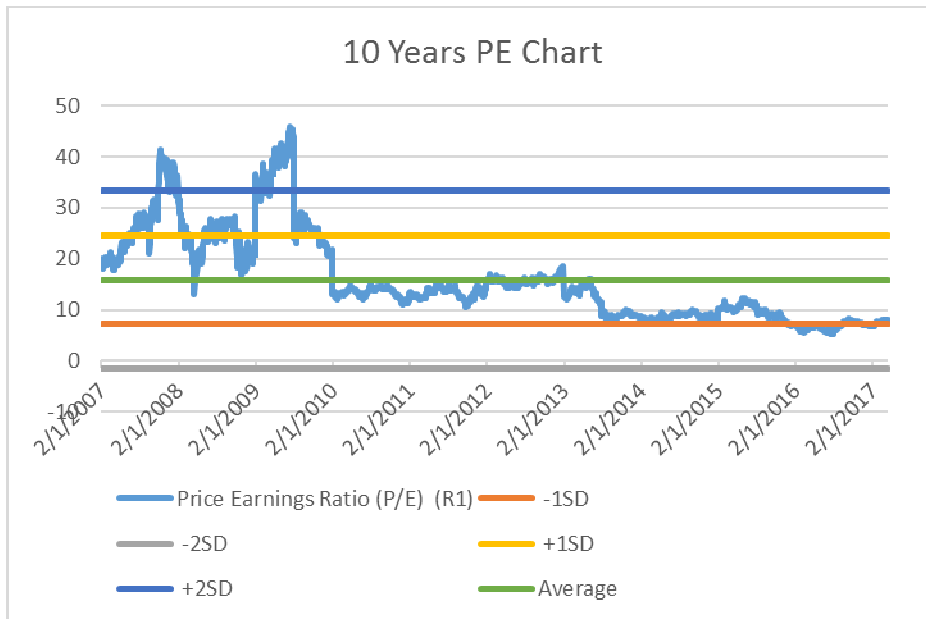
### The Valuation is attractive

The chart below shows 10 years of PB ratio of the stock, the statistic started on 5/1/2007, with 2 standard deviations.



Source: Bloomberg, Phillip Securities (HK) Research

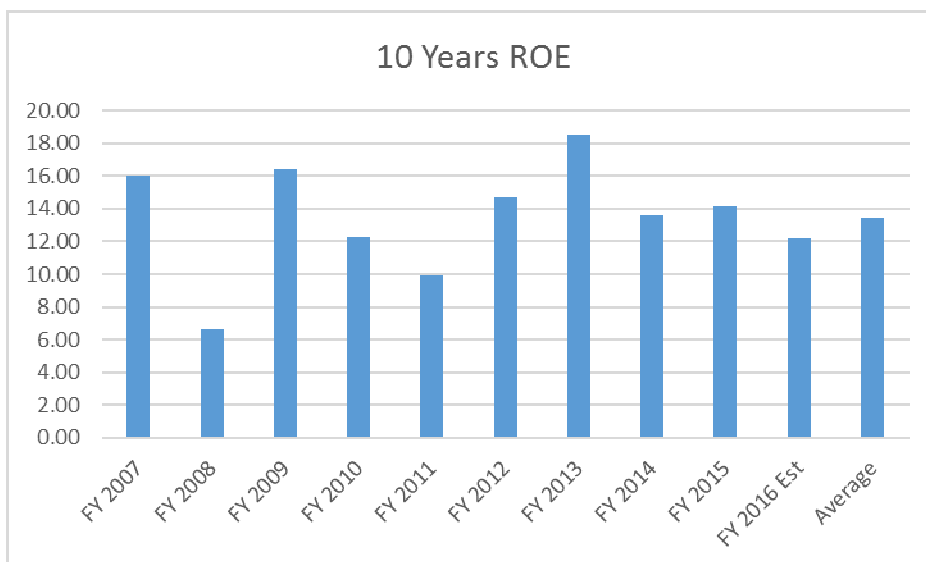
From the chart above, we can see that the PB valuation is significantly lower than the 10 years average. The average 10 years PB ratio is approximately 1.99x, one standard deviation below is 0.93x, and the stock trades significantly below the 10 years average but slightly above 1 standard deviation. From the 10 years PB chart, we can see that the valuation of the stock is extremely fluctuate, but since it is trading at significant below the 10 years average, the downside risk possibly limited. At least, in term of the PB ratio, the valuation is attractive.



Source: Bloomberg, Phillip Securities (HK) Research

From the chart above, we can see that the PE valuation is significantly lower than the 10 years average. The average 10 years PE ratio is approximately 15.89x, one standard deviation below is 7.18x, and the stock trades significantly below the 10 years average but slightly above 1 standard deviation. From the 10 years PE chart, we can see that the PE valuation of the stock is also extremely fluctuate, but since it is trading at significant below the 10 years average, in the PE point of view, the downside risk possibly limited.

The Return on Equity ratio is also crucial, which can provide more information regarding the profitability of the group. The chart in below shows the 10 years ROEs of the firm.



Source: Bloomberg, Phillip Securities (HK) Research

According to the bar chart in above, the ROE for 2016 expected to be 12.19%, which is still lower than the 10 years average ROE of 13.45%, indicating that the profitability is still acceptable for the period. Moreover, the stock trades at only around 1x PB ratio currently, which is also lower than the PB in the 2008,

but the ROE is significantly better than it was in the 2008 financial crisis period. This could indicate the stock has possibly become undervalued.

Moreover, to find out whether China Resources Power is undervalued, we used a simple Discounted Dividend Model for evaluating the intrinsic value. The annual market return of HSI that we use for the calculation is 7.16%, data collected from 31st Dec 1995 to 31st Dec 2016. We used the 10 years China government bond yield of 3.38% as the risk free rate, and the historical Beta of the stock is 0.796. From that, we calculated that the required return of the stock is 6.39%. Our prudently forecasted dividend per share for next year is 0.78 HKD per share. Based on the 10 years average ROE figure, and the dividend payout ratio will stay the same as 40.5%, we prudently estimated that the dividend growth rate is 2.72%, which is significantly lower than the country's historical GDP growth rate. As a result, we calculated the intrinsic value of HKD 21.28 per share. For the worst situation, we increase the required return of the stock by 1%, the calculated intrinsic value is still HKD 16.72 per share. Therefore, we believe that the stock is undervalued, and the downside risk of the stock is possibly limited.

### **Bottomed power consumption, coal-fired power capacity cut**

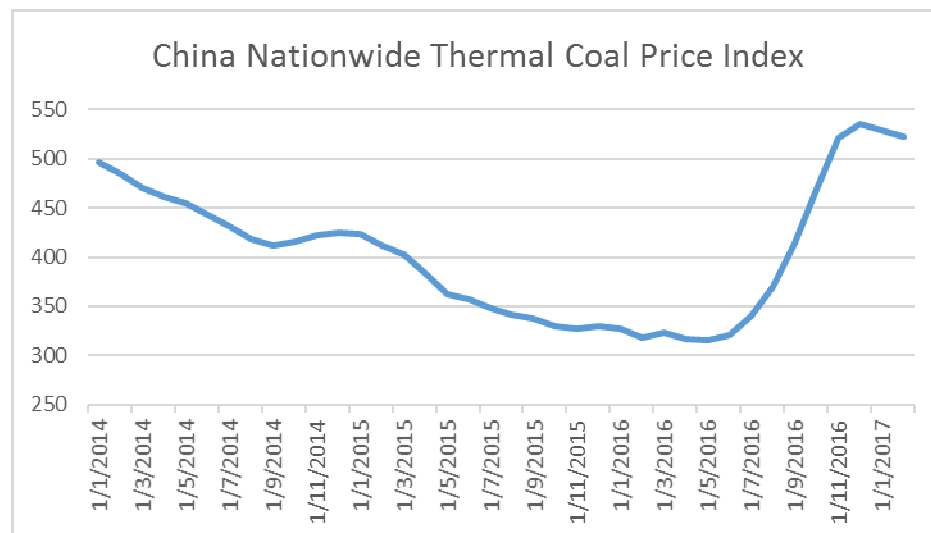
According to the China electricity council, the national total electricity consumption 5.92 trillion KWH, represents an increase of 5.0% YoY. The Power consumption rose 11 percent in the service sector and 10 percent among urban households. Meanwhile, the manufacturing and general business sector posted a 2.9 percent increase to 4.2 trillion kilowatt-hours, making it by far China's largest power consumer. Although China's economy growth slowed, and China possibly switch to less energy-intensive industries in order to be more resource-efficient, but the growth rate of the national total electricity consumption is still 5%, perhaps if the electricity consumption continue to grow steadily, the firm's long-term earning power is still favorable. In February 2017, China's overall social power consumption reached 448.8 billion kilowatt-hours (kWh), a jump of 17.2% from the same month last year. From January to February 2017, China's accumulative social power consumption reached 935.6 billion kWh, an increase of 6.3% from the same period last year, which was 4.3 percentage points higher than the previous year, according to China's National Energy Administration (NEA). This could indicate that the power consumption possibly bottomed.

Moreover, according to the annual meeting of parliament, the National Development and Reform Commission (NDRC) said it would shut or stop construction of coal-fired power plants with capacity of more than 50 million kilowatts. China moves to a greener growth model and toward use of more renewable energy resources to generate electricity, the burden for capacity cuts in coal-fired power plants will lessen. The capacity cut policy could result many smaller power generators become obsolete and further consolidate the monopoly power of the group. After the capacity cut, the on-grid coal power tariffs is expected to be increase, and the coal power average utilization hours of generating units is expected to rise as well. Overall, we believe that the coal-fired power capacity cut will be beneficial to the firm's future earning power.

### **Current China Coal Price is possibly not sustainable**

Since the China government has been implemented a successful coal supply-side structural reform, including the strictly production limitation and reduction policy in major coal producing areas, as well as intensified the inspection on illegal coal mines and closure and suspension of mines. The

China Nationwide Thermal Coal Price Index, the coal price continue to drop to 522.49 per tonne in Feb 2017. In 2016, the coal price increased roughly more than 60%, according to the data from Bloomberg. The surged coal price had a significant impact on the power of earning of the coal-fired power generation companies, no exception for China Resources Power.



Source: Bloomberg, Phillip Securities (HK) Research

However, the significant price increases disrupted the coal industry’s capacity reduction and hurt the business of downstream industries, could cause the serious excess capacity problem reappeared in the coal industry. On the demand side, the end of the winter heating season will also reduce the demand for Coal. As a result, the coal price correction would possibly continue in recent time, it is beneficial to the firm’s fuel cost reduction. As a result, along with the correction of the coal price, we believe the group’s earning power will improve in the future.

### Valuation

Taking all the points mentioned above into consideration, China Resources Power’s target price is therefore \$16.72, with Accumulate rating assigned, represents 1.05x FY16 P/B and 1.03x FY17 P/B. (Closing price as at 21 MAR 2017)

### Risks

- Risks relating to the power demand in China, the overall power demand could keep declining if the economic growth slows down.
- Risks relating to coal market, the fluctuation on the coal price will bring certain degree of risks to the fuel cost control.
- 
- Risks relating to electricity tariff, it could cause uncertainty on the firm’s revenue.
- Risks relating to environmental protection policies, the national standards for energy saving environmental protection could pushed higher and the environmental protection restrictions for energy development is possibly more tightened.

## Financials

FYE	2013	2014	2015	2016 F	2017 F
<b>Valuation Ratios</b>					
Price Earnings Ratio (P/E)	7.92	10.31	7.18	7.89	9.88
Price to Book Ratio	1.36	1.36	1.02	0.94	0.93
<b>Per share Data(HKD)</b>					
Basic Earnings per Share	2.32	1.94	2.10	1.90	1.52
Book Value per Share	13.56	14.76	14.75	15.85	16.27
Dividends per Share	0.75	0.78	0.85	0.81	0.78
<b>Growth &amp; Margins(%)</b>					
Revenue Growth	11.45	1.58	1.07	-8.76	-0.31
EPS Growth	45.91	-16.38	8.25	-0.95	-20.00
Net Income Growth	44.83	-15.74	8.41	-0.95	-20.00
Operating Profit Margin	23.30	21.03	28.21	24.89	20.17
Net Profit Margin	16.44	13.63	14.62	13.70	10.79
<b>Key Ratios</b>					
ROE	18.51	13.57	14.15	12.19	9.13
ROA	5.84	4.39	4.82	4.71	3.65
<b>Income Statement( HKD:mn)</b>					
Revenue	69,581.5	70,680.6	71,435.9	65,180.1	64,978.7
Operating Income or Losses	16,215.0	14,867.6	20,149.8	16,224.0	13,103.8
Pre-Tax Income	16,137.2	11,184.4	16,321.2	14,046.5	11,065.4
Net Income/Net Profit (Losses)	11,437.4	9,636.6	10,446.8	9,392.6	8,248.4

Source: Company reports, Phillip Securities (HK) Research Estimates

(Financial figures as at 21 Mar 2017)

**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

**GENERAL DISCLAIMER**

This publication is prepared by Phillip Securities (Hong Kong) Ltd ("Phillip Securities"). By receiving or reading this publication, you agree to be bound by the terms and limitations set out below.

This publication shall not be reproduced in whole or in part, distributed or published by you for any purpose. Phillip Securities shall not be liable for any direct or consequential loss arising from any use of material contained in this publication.

The information contained in this publication has been obtained from public sources which Phillip Securities has no reason to believe are unreliable and any analysis, forecasts, projections, expectations and opinions (collectively the "Research") contained in this publication are based on such information and are expressions of belief only. Phillip Securities has not verified this information and no representation or warranty, express or implied, is made that such information or Research is accurate, complete or verified or should be relied upon as such. Any such information or Research contained in this publication is subject to change, and Phillip Securities shall not have any responsibility to maintain the information or Research made available or to supply any corrections, updates or releases in connection therewith. In no event will Phillip Securities be liable for any special, indirect, incidental or consequential damages which may be incurred from the use of the information or Research made available, even if it has been advised of the possibility of such damages.

Any opinions, forecasts, assumptions, estimates, valuations and prices contained in this material are as of the date indicated and are subject to change at any time without prior notice.

This material is intended for general circulation only and does not take into account the specific investment objectives, financial situation or particular needs of any particular person. The products mentioned in this material may not be suitable for all investors and a person receiving or reading this material should seek advice from a financial adviser regarding the suitability of such products, taking into account the specific investment objectives, financial situation or particular needs of that person, before making a commitment to invest in any of such products.

This publication should not be relied upon as authoritative without further being subject to the recipient's own independent verification and exercise of judgment. The fact that this publication has been made available constitutes neither a recommendation to enter into a particular transaction nor a representation that any product described in this material is suitable or appropriate for the recipient. Recipients should be aware that many of the products which may be described in this publication involve significant risks and may not be suitable for all investors, and that any decision to enter into transactions involving such products should not be made unless all such risks are understood and an independent determination has been made that such transactions would be appropriate. Any discussion of the risks contained herein with respect to any product should not be considered to be a disclosure of all risks or a complete discussion of such risks.

Nothing in this report shall be construed to be an offer or solicitation for the purchase or sale of a security. Any decision to purchase securities mentioned in this research should take into account existing public information, including any registered prospectus in respect of such security.

**Disclosure of Interest**

Analyst Disclosure: Neither the analyst(s) preparing this report nor his associate has any financial interest in or serves as an officer of the listed corporation covered in this report.

Firm's Disclosure: Phillip Securities does not have any investment banking relationship with the listed corporation covered in this report nor any financial interest of 1% or more of the market capitalization in the listed corporation. In addition, no executive staff of Phillip Securities serves as an officer of the listed corporation.

**Availability**

The information, tools and material presented herein are not directed, intended for distribution to or use by, any person or entity in any jurisdiction or country where such distribution, publication, availability or use would be contrary to the applicable law or regulation or which would subject Phillip Securities to any registration or licensing or other requirement, or penalty for contravention of such requirements within such jurisdiction.

Information contained herein is based on sources that Phillip Securities (Hong Kong) Limited ("PSHK") believed to be accurate. PSHK does not bear responsibility for any loss occasioned by reliance placed upon the contents hereof. PSHK (or its affiliates or employees) may have positions in relevant investment products. For details of different product's risks, please visit the Risk Disclosures Statement on <http://www.phillip.com.hk>.

© 2017 Phillip Securities (Hong Kong) Limited

**Contact Information (Regional Member Companies)**



**SINGAPORE**

**Phillip Securities Pte Ltd**  
Raffles City Tower  
250, North Bridge Road #06-00  
Singapore 179101  
Tel : (65) 6533 6001  
Fax : (65) 6535 6631  
Website: [www.poems.com.sg](http://www.poems.com.sg)

**HONG KONG**

**Phillip Securities (HK) Ltd**  
Exchange Participant of the Stock Exchange of Hong Kong  
11/F United Centre 95 Queensway  
Hong Kong  
Tel (852) 22776600  
Fax (852) 28685307  
Websites: [www.phillip.com.hk](http://www.phillip.com.hk)

**INDONESIA**

**PT Phillip Securities Indonesia**  
ANZ Tower Level 23B,  
Jl Jend Sudirman Kav 33A  
Jakarta 10220 – Indonesia  
Tel (62-21) 57900800  
Fax (62-21) 57900809  
Website: [www.phillip.co.id](http://www.phillip.co.id)

**THAILAND**

**Phillip Securities (Thailand) Public Co. Ltd**  
15th Floor, Vorawat Building,  
849 Silom Road, Silom, Bangrak,  
Bangkok 10500 Thailand  
Tel (66-2) 6351700 / 22680999  
Fax (66-2) 22680921  
Website: [www.phillip.co.th](http://www.phillip.co.th)

**UNITED KINGDOM**

**King & Shaxson Capital Limited**  
6th Floor, Candlewick House,  
120 Cannon Street,  
London, EC4N 6AS  
Tel (44-20) 7426 5950  
Fax (44-20) 7626 1757  
Website: [www.kingandshaxson.com](http://www.kingandshaxson.com)

**AUSTRALIA**

**PhillipCapital Australia**  
Level 12, 15 William Street,  
Melbourne, Victoria 3000, Australia  
Tel (613) 96188238  
Fax (613) 92002272  
Website: [www.phillipcapital.com.au](http://www.phillipcapital.com.au)

**MALAYSIA**

**Phillip Capital Management Sdn Bhd**  
B-3-6 Block B Level 3 Megan Avenue II,  
No. 12, Jalan Yap Kwan Seng, 50450  
Kuala Lumpur  
Tel (603) 21628841  
Fax (603) 21665099  
Website: [www.poems.com.my](http://www.poems.com.my)

**JAPAN**

**PhillipCapital Japan K.K.**  
Nagata-cho Bldg.,  
8F, 2-4-3 Nagata-cho,  
Chiyoda-ku, Tokyo 100-0014  
Tel (81-3) 35953631  
Fax (81-3) 35953630  
Website: [www.phillip.co.jp](http://www.phillip.co.jp)

**CHINA**

**Phillip Financial Advisory (Shanghai) Co. Ltd**  
No 436 Hengfeng Road,  
Greentech Unit 604,  
Postal code 200070  
Tel (86-21) 51699400  
Fax (86-21) 63532643  
Website: [www.phillip.com.cn](http://www.phillip.com.cn)

**FRANCE**

**King & Shaxson Capital Limited**  
3rd Floor, 35 Rue de la Bienfaisance 75008  
Paris France  
Tel (33-1) 45633100  
Fax (33-1) 45636017  
Website: [www.kingandshaxson.com](http://www.kingandshaxson.com)

**UNITED STATES**

**Phillip Futures Inc**  
141 W Jackson Blvd Ste 3050  
The Chicago Board of Trade Building  
Chicago, IL 60604 USA  
Tel +1.312.356.9000  
Fax +1.312.356.9005