

Grandblue ENV (600323.SH)

Solid Waste Disposal Business Is Accelerating Its Expansion

Hong Kong | Environmental Protection | Company report

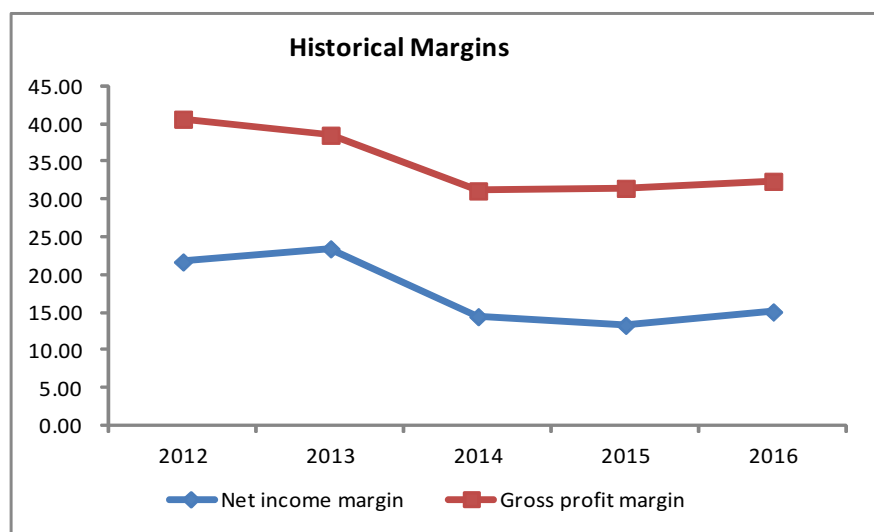
21 June 2017

Stable Operation Promotes Greater Profitability

In 2016, the company's revenue jumped by 9.93% yoy to RMB3.69 billion; the net profit excluding non-recurring items increased by 31.8% yoy to RMB493 million, and the earnings of non-recurring items per share was RMB0.64. The company basically finished its annual objectives. In the first quarter of 2017, the company's revenues increased by 14.57% yoy to RMB945 million; the net profit excluding non-recurring items grew by 16.5% yoy to RMB122 million, which were in line with expectations. In the past five years from 2012 to 2016, the company recorded sustainable growth: the compound growth rate of the company's revenue reached 33%, and the compound growth rate of net profit attributable to the parent company reached 21.7%.

Specifically, the revenue from solid waste disposal business and water supply business increased by 32.6%, 23%, respectively, and with revenue share of 36% and 23.3%, respectively; the revenue from gas business and sewage disposal business decreased by 13.3% and 7.8%, respectively, and with revenue share of 31.5% and 4.3%, respectively, due to the influence of synchronized down-regulation of gas's selling price with procurement price and VAT policy adjustment, respectively.

The fact that the company's increase of revenue is greater than that of income mainly benefits from strict control over expenses. The increase of expenses was 8.5%, lower than the increase of income. The total expenses of the three items were RMB543 million, and the expense ratio was 14.7%; the expenses last year on the same period was RMB 539 million, and the expense ratio was 16.1%. The expense ratio declined 1.4% yoy, and brought the overall gross margin with an increase of nearly 1%, and net profit margin with an increase of 1.4%.



Source: Wind, Phillip Securities(HK)Research

Buy

CMP: RMB 14.41

(Closing price as at 19 June 2017)

TARGET: HKD 19.00 (31.8%)

COMPANY DATA

O/S SHARES (MN) :	766
MARKET CAP (RMB MN) :	11,042
52 - WK HI/LO (RMB):	16.28/11.88

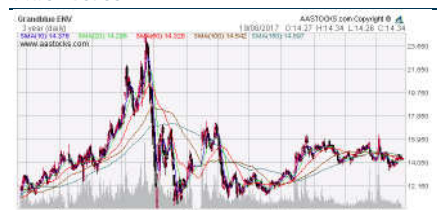
SHARE HOLDING PATTERN , %

Foshan nanhai water supply group co., LTD	17.98
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PRICE PERFORMANCE , %

	1-Month	3-Month	1-Year
Grandblue ENV	4.01	-2.59	16.99
SSE	1.05	-3.53	8.25

PRICE VS. SSE



Source: Phillip Securities (HK) Research

KEY FINANCIALS

RMBmn	FY15	FY16	FY17E	FY18E
Revenue	3,357	3,690	4,140	5,026
Net Profit	403	509	604	736
P/E, x	27.2	21.8	18.3	15.0
EPS, RMB	0.53	0.66	0.79	0.96
P/B, x	2.5	2.3	2.2	2.0
BVPS, RMB	5.74	6.30	6.71	7.30
ROE, %	9.2	10.5	11.8	13.2

Source: Company reports, Phillip Securities Est.

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Solid Waste Disposal Business Is Accelerating Its Expansion; Other Businesses Are Making Steady Progress

In this year, revenue share of solid waste disposal business continued to grow to 36% (+6%), becoming the primary drive for earnings growth; gross margin declined by 3% to 39.86%, mainly influenced by VAT adjustment. C&G China, consolidated in 2015, made contributions of RMB132 million net profit excluding non-recurring items, failing to accomplish its performance commitment of RMB164 million. This is mainly because the time delay of projects in Langfang in Hebei province and Dalian, and the project in Dalian will be put into operation in the first half year of 2017.

In the aspects of project operation, in 2016, the company acquired the Zhangzhou waste incineration project with 1000 tons per day by, added 3000 tons per day in Shunde Solid Waste Industrial Park, and signed the framework agreement for purchasing 70% equity of Weichen Environment. If implemented smoothly, the project will contribute to hazardous waste disposal with newly added capacity of 220 thousand tons per year. In the first half year of 2017, it is expected to win the bidding on solid waste PPP project in Kaiping worth RMB527 million, adding a capacity of 1500 tons per day on waste incineration, and RMB 850 million will be invested to make technical transformation and capacity expansion on Hainan Solid Waste Industrial Park, the three factories in Hainan are thus expected to add a capacity of 1500 tons per day. At present, the company's business scales of waste to energy, sludge disposal and food waste are 21,350 tons per day, 1,350 tons per day and 1,150 tons per day, respectively. Among them, scales of planned projects and designated projects are 10,050 tons per day, they are expected to make contributions to performance in 2018 and beyond, and the affluent project stock will become solid pillars of business growth in the next three years.

Summary of the project to be built

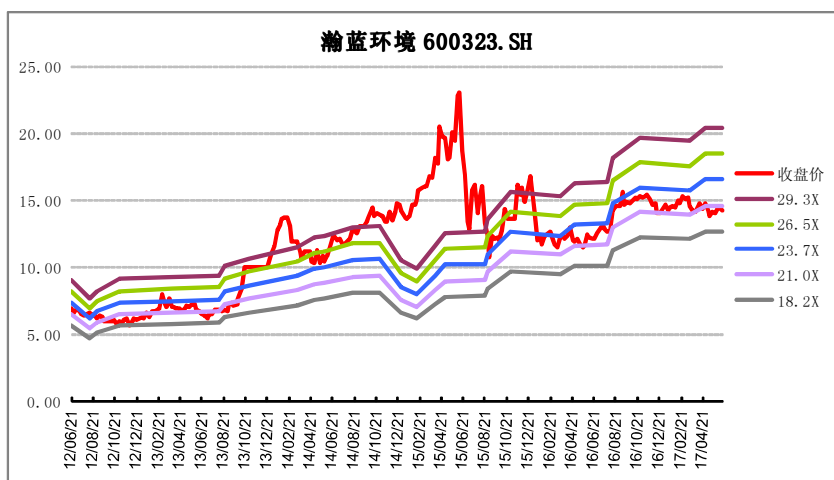
	Get project time	Size(Tons/day)
孝感垃圾焚燒項目一期和二期	2010.4	1050
貴陽垃圾焚燒項目	2013.5	2000
漳州垃圾焚燒項目	2016.2	1000
順德固廢產業園	2016.9	3000
開平固廢PPP項目	2017.4	1500
南海垃圾焚燒三廠項目	2017.4	1500
Total		10050

Source: Company report, Phillip Securities(HK)Research

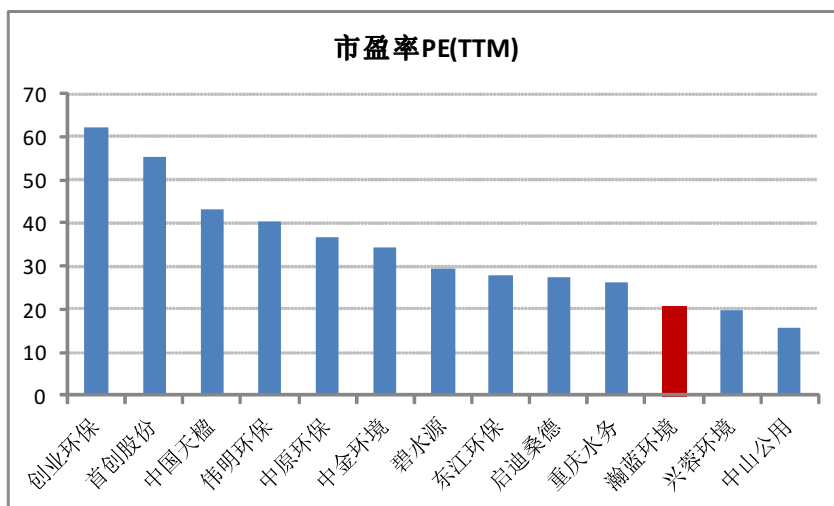
The company's gas business, water supply business and sewage business focus mainly on Nanhai District, Foshan, having a respectively dominant position in the district. Influenced by price fluctuation in gas market, the gas business suffered declination for the first time, but it still over-fulfilled its yearly performance commitment with RMB172 million net profit. In the meantime, gas business successfully expanded beyond Foshan, and gained the gas franchise in 11 towns and countries in Zhangshu, Jiangxi province, by purchasing 70% equity of GrandBlue Energy. The huge increase in performance of water supply business during the period benefited from consolidated Qiaonan Water Supply and 15% increase in water price, and its gross margin grew by 2.2%. It is expected that water supply business will continue to maintain stable operation, and provide a steady capital flow for the company. Influenced by VAT adjustment, the gross margin of sewage disposal business dropped by 5.6%, and the revenue and profitability continued to decline.

Valuation and Rating

We are optimistic about the strategic development direction of expansions centered around solid waste disposal business, and we will stay focused on the solid waste disposal business development and market mergers and acquisitions. We expect that the company's revenues in 2017-2018 will reach RMB 4140million and RMB 5030 million, respectively; net profits will be RMB 604 million and RMB 736 million, respectively; EPS will be RMB 0.79 and RMB 0.96, respectively. The current estimate value is much less than the average PE ratio in the last five years(26.9x), and is at a low level among the industry. So based on the 24x PE in 2017, we give a target price of RMB 19.0, and the rating is "Buy". (Closing price as at 19 June 2017)



Source: Wind, Phillip Securities(HK)Research



Source: Wind, Phillip Securities(HK)Research

Risk Warnings

- Increasingly severe market competition;
- Project expansion falling short of expectations;
- Under-funding risks;
- Industrial policy risks.

Financials

FYE	FY14	FY15	FY16	FY17E	FY18E
Valuation Ratios					
P/E	29.41	27.19	21.83	18.26	15.01
P/B	3.32	2.51	2.29	2.15	1.97
Per share data(RMB)					
EPS,Adj+	0.49	0.53	0.66	0.79	0.96
BVPS	4.35	5.74	6.30	6.71	7.30
Growth & Margins(%)					
Growth					
Revenue	243.2%	37.8%	9.9%	12.2%	21.4%
Operating income	70.9%	9.6%	22.5%	20.6%	29.0%
Net profit	32.0%	30.5%	26.2%	18.8%	21.7%
Margins					
Gross profit margin	31.1%	31.5%	32.4%	32.5%	33.0%
Operating profit margin	18.6%	14.8%	16.5%	17.8%	18.9%
Net income margin	12.7%	12.0%	13.8%	14.6%	14.6%
Key Ratios					
ROE(%)	9.3%	9.2%	10.5%	11.8%	13.2%
ROA(%)	3.8%	3.5%	4.0%	4.3%	4.7%
Income Statement(RMB mn)					
Revenue	2,435	3,357	3,690	4,140	5,026
- Cost of Goods Sold	1,678	2,300	2,495	2,794	3,367
Gross Income	758	1,057	1,195	1,346	1,659
- Operating Expenses	287	539	543	563	653
Operating Income	454	498	609	735	948
- Net Non-Operating Losses (Gains)	(13)	(78)	(139)	(125)	(95)
Pretax Income	467	576	749	860	1,043
- Income Tax Expense	116	130	192	211	256
Net profit	309	403	509	604	736

Source: Company, Phillip Securities (HK) Research Estimates
 (Financial figures as at 19 June 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

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