

ZFET Co.,Ltd. (002479.SZ)

Slowed down in Q3, yet the growth of annual result can still be expected

Hong Kong | Environmental Protection | Company report

15 November 2017

Summary of Investment

-Senior management holds more shares to show confidence, and private placement was approved by the China Securities Regulatory Commission.

-The growth of annual result is highly certain;

Investment Rating

The influence of share issuance isn't considered temporarily, and it is predicted that the net profits of the Company of 2017 and 2018 will be 370, 481 million; the EPS is 0.47, and 0.48; the P/E ratio will be 23.4 times and 18.6 times, respectively. The rating of "Buy" is given. (Closing price as at 13 Nov 2017)

Historical P/E valuation



Source: Wind, Phillip Securities(HK)Research

Buy

CMP: RMB 10.88

(Closing price as at 13 Nov 2017)

TARGET: RMB 15.00 (38%)

COMPANY DATA

O/S SHARES (MN) :	796
MARKET CAP (RMB MN) :	8,664
52 - WK HI/LO (RMB):	16.58/10.51

SHARE HOLDING PATTERN , %

Zhejiang fuchunjiang communication group co. LTD	38.0
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PRICE PERFORMANCE , %

	1-Month	3-Month	1-Year
ZFET Co.,Ltd	-6.37	-2.60	-26.36
SSE	1.24	6.99	7.40

PRICE VS. SSE



Source: Phillip Securities (HK) Research

KEY FINANCIALS

RMBmn	FY15	FY16	FY17E	FY18E
Revenue	2,877	2,699	3,415	4,166
Net Profit	181	245	370	481
P/E,x	45.3	35.1	23.4	18.6
EPS, RMB	0.24	0.31	0.47	0.58
P/B, x	3.2	3.0	2.8	2.0
BVPS, RMB	3.4	3.6	4.0	5.4
ROE, %	6.6	8.6	11.8	10.9

Source: Company reports, Phillip Securities Est.

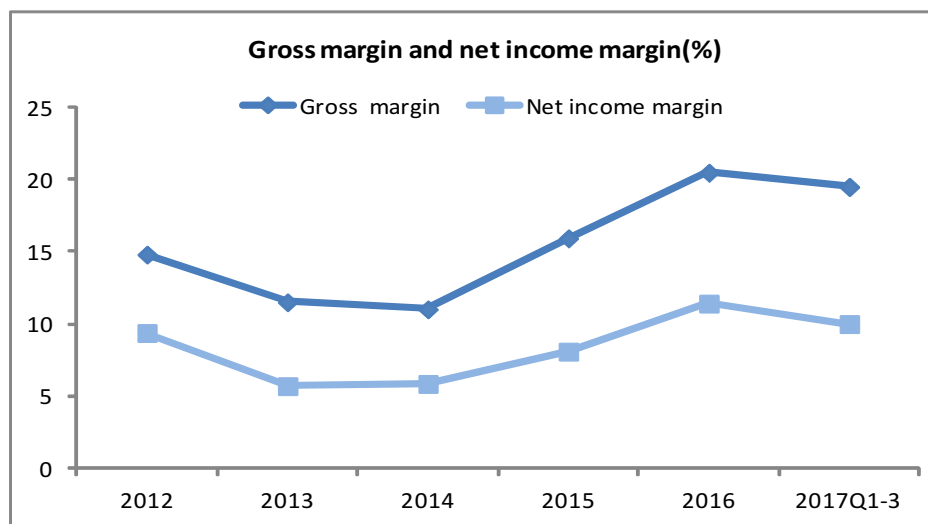
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The net profit declined slightly in Q3. According to the reports of the first three quarters of 2017, FC Environment recorded a revenue of RMB2,476 million, up by about 33% YoY. Net profit attributable to parent company was RMB248 million, up by 37.3% YoY and up by 43.3% YoY after deduction of non-recurring profit and loss. EPS was RMB0.31. Specifically, Q1, Q2 and Q3 reported revenues of RMB793 million (+20%), RMB913 million (+41%) and RMB769 million (+39%), respectively, and net profits after deduction of non-recurring profit and loss of RMB79 million (+87%), RMB113 million (+53%) and RMB49 million (-5.9%), respectively. In general, Q3's revenue grew rapidly, and the net profit decreased slightly YoY. The main reason is the rise of prices of raw materials and the influence of environmental protection supervision on the downstream users' demands.



Source: Wind, Phillip Securities(HK)Research

The Company predicted that the net profit attributable to parent company of the year will be RMB318 to RMB392 million, up by 30%-60% YoY. The annual result growth mainly comes from the facts that the Company has carried out the new Coal Heat Linkage Mechanism in the Fuyang Base and increased the heat supply price, and the productivity of newly constructed project has been gradually released. Correspondingly, in Q4 the Company reported net profit of RMB70 million to RMB144 million, a y-o-y increase of 9.3%-125%, which is higher than that of Q3. It is predicted that the short-term influence of environmental protection supervision will be gradually alleviated, and the downstream users' demands may gradually recover.

Rise of coal price led to the reduction of gross margin. With regard to profitability, as a result of the rise of prices of raw materials, the gross margin decreased by 2.3% to 19.5% YoY; the net profit is 10%, basically the same YoY. The net cash flow of operating activity decreased by 8.7% YoY, mainly because of the increase of the cash paid for raw materials. Specifically, the net cash flow for the operating activities in Q3 was RMB334 million, up by 60.1% YoY and up by 106% QoQ. Thus, the cash flow-back has improved quarter by quarter.

Senior management consecutively holds more shares to show their confidence in the Company's development. From July to September 2017, the Company's President Secretary Mr. Zhang Jie, Director and General Manager Mr. Zhang Zhongmei and Director Mr. Wu Bin increased total shareholding by 2.6 million shares at the price of 10.86-12.26, namely RMB30 million in total, accounting for 3.26% of the total share capital. The current price has a high safety margin.

Private placement was approved by the China Securities Regulatory Commission.

On September 28, 2017, the Company's application for private placement of A-shares in 2016 was examined and approved by the Issuance Examination Commission of China Securities Regulatory Commission. This private placement planned to raise RMB920 million, of which 65% is used for the acquisition of 30% equity interest of Xingang Thermal Power and the Expansion Project of Xingang Thermal Power, and the remaining the Transformation Project of Flue Gas Treatment Technology, and the Technological Transformation Project of Combustion System and the Cogeneration Project in the North of Liyang City. After private placement, it is expected that the Company's revenue and profit scale will largely increase, and endogenous growth can be expected in the long run.

Risk Warnings

Macroeconomic and policy risks;

Risks of rise of coal price and continual decrease of gross margin;

Production of newly added project lower than expected;

Risk of private placement below expectations;

Financials

FYE	FY14	FY15	FY16	FY17E	FY18E
Valuation Ratios					
P/E	45.33	45.33	35.10	23.38	18.63
P/B	3.96	3.17	3.03	2.75	2.03
Dividend Yield	1.2%	1.4%	0.9%	1.3%	1.6%
Per share data(RMB)					
EPS,Adj+	0.24	0.24	0.31	0.47	0.58
BVPS	2.74	3.43	3.59	3.95	5.36
Dividend Per Share	0.13	0.15	0.10	0.14	0.18
Growth & Margins(%)					
Growth					
Revenue	17.8%	-22.9%	-6.2%	26.5%	22.0%
Operating income	30.1%	4.6%	24.3%	69.1%	33.5%
Net profit	20.8%	5.0%	35.0%	51.2%	29.7%
Margins					
Gross profit margin	11.0%	15.9%	20.5%	20.0%	20.4%
Operating profit margin	6.6%	8.9%	11.8%	15.8%	17.3%
Net income margin	4.6%	6.3%	9.1%	10.8%	11.5%
Key Ratios					
ROE(%)	7.9%	6.6%	8.6%	11.8%	10.9%
ROA(%)	4.7%	4.1%	4.8%	7.2%	8.3%
Income Statement(RMBmn)					
Revenue	3,730	2,877	2,699	3,415	4,166
- Cost of Goods Sold	3,319	2,418	2,147	2,732	3,316
Gross Income	411	458	553	683	850
- Operating Expenses	165	201	233	142	128
Operating Income	246	257	320	541	722
- Net Non-Operating Losses (Gains)	(22)	(33)	(54)	16	53
Pretax Income	268	290	374	525	669
- Income Tax Expense	49	57	66	89	114
Net profit	173	181	245	370	481

Source: Company, Phillip Securities (HK) Research Estimates
(Financial figures as at 13 Nov 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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