

BJ ENT WATER (371.HK)

Results of 1H2019 in Line, Asset-Light Transformation is Expected

Hong Kong | Environmental Protection | Company Update

September 10, 2019

Company Update

For the six months ended 30 June 2019, the company's revenue was HKD 12.829 billion (corresponding period in 2018: HKD 10.009 billion), representing an increase of 28.18%. Revenue from Sewage and reclaimed water treatment services was HKD 2.513 billion (corresponding period in 2018: HKD 2.064 billion), representing an increase of 21.79%. Revenue from Water distribution services was HKD 1.173 billion (corresponding period in 2018: HKD 1.015 billion), representing an increase of 15.62%. Revenue from Construction services was HKD 7.94 billion (corresponding period in 2018: HKD 5.752 billion), representing an increase of 38.04%. Revenue from Construction services for comprehensive renovation projects was HKD 3.221 billion (corresponding period in 2018: HKD 2.463 billion), representing an increase of 30.77%. Revenue from Construction of BOT water projects for comprehensive renovation projects was HKD 4.719 billion (corresponding period in 2018: HKD 3.298 billion), representing an increase of 43.48%. Revenue from Technical services and sale of machineries for the water environmental renovation for comprehensive renovation projects was HKD 1.203 billion (corresponding period in 2018: HKD 1.179 billion), representing an increase of 2.07%. The gross profit was HKD 4.771 billion (corresponding period in 2018: HKD 3.834 billion), representing an increase of 24.49%. The GP margin was 37.10%, decreasing by 1.1 ppt compared with 1H2018, which is mainly due to the change of revenue portfolios. Profit attributable to equity holders of the company was HKD 2.77 billion (corresponding period in 2018: HKD 2.366 billion), representing an increase of 17.06%. Basic and diluted earnings per share were HK28.68 cents and 28.25 cents respectively. The interim dividend of HK10.7 cents per ordinary share for the six months ended 30 June 2019 (six months ended 30 June 2018: HK9.5 cents per ordinary share), showing an increase of 12.63%, the payout ratio is 37%, same as 1H2018.

The company's performance of core business is basically consistent with our forecast, related performance increase in total revenue was mainly contributed from the increase of water treatment services and construction services for the water environmental renovation. Total daily design capacity for new projects secured for the period was 1,355,925 ton, the net increase in total daily design capacity of the period was 936,925 tons, less than the company's guidance of 4 million tons additional for the full 2019. But the company maintain the above new capacity target, believing there will be more opportunities of M&A in 2H2019.

Stable growth in production capacity, waiting for high quality M&A opportunities

As at 30 June 2019, the company entered into service concession arrangements and entrustment agreements for a total of 1,047 water plants including 875 sewage treatment plants, 140 water distribution plants, 30 reclaimed water treatment plants and 2 seawater desalination plants. Total daily design capacity for new projects secured for the period was 1,355,925 tons including BOT projects of 130,000 tons, PPP projects of 882,925 tons, entrustment operation projects of 263,000 tons, and 80,000 tons through mergers and acquisitions. Due to different reasons such as expiration of projects, the company exited projects with aggregate daily design capacity of 419,000 tons during the period. As such, the net increase in daily design capacity of the period was 936,925 tons. As at 30 June 2019, total daily design capacity was 37,761,558 tons. The company's production capacity has maintained a compound annual growth of 35.96% since 2008. Although the progress of new projects in 1H2019 has slowed down, we are still optimistic about the company's capacity growth in 2H2019. We expect that the company will achieve the goal of adding 4 million tons of new capacity in 2019 through more M&A projects.

BUY

CMP HKD 4.26

(Closing price at 6 September 2019)

TARGET HKD 5.83 (+36.76%)

COMPANY DATA

O/S SHARES (MN)	9,658.9
MARKET CAP (HKDMN)	42,675
52 - WK HI/LO (HKD):	3.74/5.09

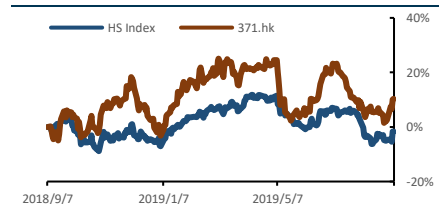
SHARE HOLDING PATTERN

BE Environment	41.17%
CN Yangtze Power Intl (HK) Ltd	6.00%

PRICE PERFORMANCE

	1M	3M	1Y
BJ ENT WATER	5.97%	3.90%	9.78%
HSI	2.75%	-1.02%	-1.05%

RETURN & HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

mn HKD	FY17 A	FY18 A	FY19 E	FY20 E	FY21 E
Revenue	21,192	24,597	28,030	31,484	35,562
NP for Owners	3,717	4,471	5,591	6,264	7,177
EPS HKD	0.42	0.48	0.58	0.63	0.71
P/E	10.04	8.89	7.36	6.72	6.00
BVPS HKD	2.37	2.73	2.99	3.32	3.68
P/B	1.80	1.56	1.42	1.28	1.16
ROE	19.94%	19.33%	20.55%	20.31%	20.52%

Source: Company reports, Phillip Securities Est.

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Continue asset-light transformation, closely cooperate with the Three Gorges Group

On January 18, 2019, the company entered into a subscription agreement with China Yangtze Power International, which has conditionally agreed to subscribe for 470,649,436 new ordinary shares. This means that the company will further deepen its partnership with China Three Gorges Corporation, to develop water environmental protection business in the Yangtze River area. In addition, the company also adheres to the “dual-platform strategy” and asset-light business model. It is expected that there will be a new signed RMB 20 billion water environment renovation projects and a capital expenditure of HKD 12 billion for the whole year. The interest expense for 1H2019 has also increased 42.73% to HKD 1.193 billion, the gearing ratio dropped from 114% to 110%. However, we expect that as the company's asset-light model continues to promote, the future capital expenditure will gradually decline, and the financial situation will further improve.

Figure-1: Profitability level

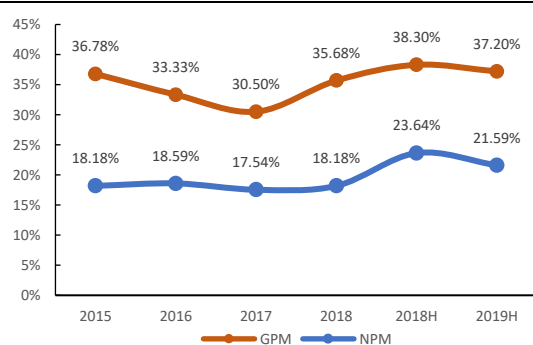
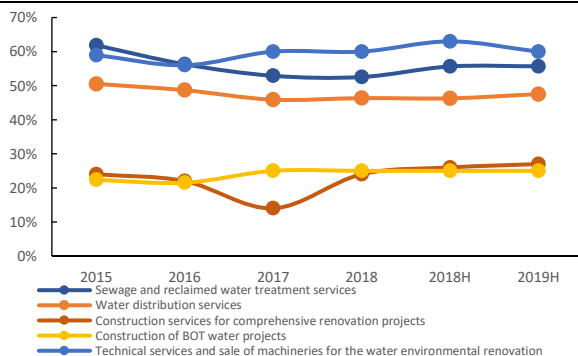


Figure-2: GPM of segments



Source: Phillip Securities (HK) Research, Company Report

Table-1: Financial performance of last five years

HKD in million		2015A	2016A	2017A	2018A	2018H	2019H
Water Treatment Services	Revenue	3,515.10	3,653.90	4,031.70	4,644.50	2,063.63	2,513.21
	YoY		3.95%	10.34%	15.20%		21.79%
	COS	1,340.65	1,596.65	1,898.74	2,204.23	915.31	1,113.72
	GPM	61.86%	56.30%	52.90%	52.54%	55.65%	55.69%
	NP Attributable to Shareholders	1,616.30	1,697.00	1,757.40	2,099.00	988.10	1,230.80
	NP Margin	45.98%	46.44%	43.59%	45.19%	47.88%	48.97%
	Revenue	881.10	1,371.40	1,839.70	2,341.90	1,014.79	1,173.32
	YoY		55.65%	34.15%	27.30%		15.62%
	COS	435.81	703.79	995.49	1,256.39	545.06	615.63
	GPM	50.54%	48.68%	45.89%	46.35%	46.29%	47.53%
NP Attributable to Shareholders	409.30	578.50	690.00	849.30	298.80	456.30	
NP Margin	46.45%	42.18%	37.51%	36.27%	29.44%	38.89%	
Sub-total	Revenue	4,396.20	5,025.30	5,871.40	6,986.40	3,078.42	3,686.53
YoY			14.31%	16.84%	18.99%		19.75%
COS	1,776.46	2,300.44	2,894.23	3,460.62	1,460.37	1,729.35	
GPM	59.59%	54.22%	50.71%	50.47%	52.56%	53.09%	
Construction services for the water environmental renovation	Revenue	1,889.70	4,612.30	7,335.30	6,606.90	2,463.20	3,221.20
	YoY		144.08%	59.04%	-9.93%		30.77%
	COS	1,436.17	3,597.59	6,308.36	5,021.24	1,822.77	2,351.48
	GPM	24.00%	22.00%	14.00%	24.00%	26.00%	27.00%
	NP Attributable to Shareholders	396.20	786.60	1,045.50	1,398.90	812.90	908.50
	NP Margin	20.97%	17.05%	14.25%	21.17%	33.00%	28.20%
	Revenue	6,441.30	6,696.30	6,647.10	8,698.60	3,288.70	4,718.50
	YoY		3.96%	-0.73%	30.86%		43.48%
	COS	5,001.13	5,255.58	4,985.33	6,523.95	2,466.53	3,538.88
	GPM	22.36%	21.52%	25.00%	25.00%	25.00%	25.00%
NP Attributable to Shareholders	894.70	1,113.30	1,133.40	1,654.10	593.40	861.90	
NP Margin	13.89%	16.63%	17.05%	19.02%	18.04%	18.27%	
Sub-total	Revenue	8,331.00	11,308.60	13,982.40	15,305.50	5,751.82	7,939.69
YoY			35.74%	23.64%	9.46%		38.04%
COS	6,437.30	8,853.18	11,293.68	11,545.19	4,289.29	5,890.35	
GPM	22.73%	21.71%	19.23%	24.57%	25.43%	25.81%	
Technical services and sale of machineries for the water environmental renovation	Revenue	775.80	1,020.90	1,338.60	2,305.00	1,178.51	1,202.89
	YoY		31.59%	31.12%	72.19%		2.07%
	COS	318.08	449.20	535.44	922.00	436.05	481.16
GPM	59.00%	56.00%	60.00%	60.00%	63.00%	60.00%	

	NP Attributable to Shareholders	264.40	274.90	506.20	773.00	348.50	356.80
	NP Margin	34.08%	26.93%	37.82%	33.54%	29.57%	29.66%
Total	Total Revenue	13,502.96	17,354.83	21,192.37	24,596.86	10,008.75	12,829.12
	YoY		28.53%	22.11%	16.06%		28.18%
	COS adj	8,536.06	11,569.99	14,727.85	15,820.92	6,175.25	8,056.93
	GPM	36.78%	33.33%	30.50%	35.68%	38.30%	37.20%
	NP Attributable to Shareholders adj	2,455.37	3,227.01	3,717.23	4,471.27	2,366.12	2,769.86
	NP Margin	18.18%	18.59%	17.54%	18.18%	23.64%	21.59%

Source: Phillip Securities (HK) Research, Company Report

Table-2: Results of 1H2019

mn HKD	2018H	2019H	YoY Growth
Segment Analysis			
Sewage and reclaimed water treatment services			
Revenue	2,063.63	2,513.21	21.8%
GPM	56%	56%	+0ppt
NP Attributable to Shareholders Margin	48%	49%	+1ppt
Water distribution services			
Revenue	1,014.79	1,173.32	15.6%
GPM	46%	48%	+1ppt
NP Attributable to Shareholders Margin	29%	39%	+9ppt
Construction services for comprehensive renovation projects			
Revenue	2,463.20	3,221.20	30.8%
GPM	26%	27%	+1ppt
NP Attributable to Shareholders Margin	33%	28%	-5ppt
Construction of BOT water projects			
Revenue	3,288.70	4,718.50	43.5%
GPM	25%	25%	+0ppt
NP Attributable to Shareholders Margin	18%	18%	+0ppt
Technical services and sale of machineries for the water environmental renovation			
Revenue	1,178.51	1,202.89	2.1%
GPM	63%	60%	-3ppt
NP Attributable to Shareholders Margin	30%	30%	+0ppt
P&L Analysis			
Total Revenue	10,008.75	12,829.12	28.2%
COS	-6,175.25	-8,056.93	30.5%
GP	3,833.50	4,772.18	24.5%
SG&A	-966.69	-1,115.94	15.4%
Operating Profit	2,866.81	3,656.24	27.5%
Net Other Income	1,134.81	1,292.56	13.9%
EBIT	4,001.62	4,948.80	23.7%
Net Interest Expense	-622.18	-884.15	42.1%
EBT	3,379.44	4,064.65	20.3%
Tax	-609.20	-771.15	26.6%
NP	2,770.24	3,293.50	18.9%
Holders of Perpetual Capital Instruments	126.51	120.15	-5.0%
Minority Interest	277.62	403.50	45.3%
NP attributable to shareholders	2,366.12	2,769.86	17.1%
EPS (Basic)	0.26	0.29	12.1%
EPS (Diluted)	0.25	0.28	12.2%
Margin Analysis			
Gross Margin	38%	37%	-1ppt
Operating Margin	29%	28%	+0ppt
Net Margin	24%	22%	-2ppt
Effective Tax Rate	18%	19%	+1ppt

Source: Phillip Securities (HK) Research, Company Report

Figure-3: Forward P/E Band

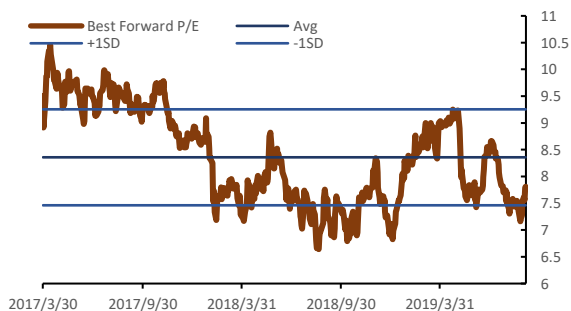
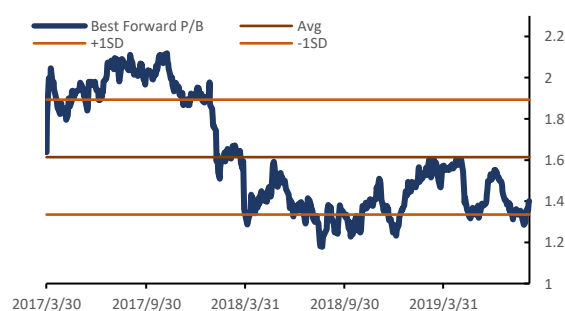


Figure-4: Forward P/B Band



Source: Phillip Securities (HK) Research, Bloomberg

Table-3: Key Actual Figures and Forecast

mn HKD	2019H	Previous 2019 Forecast	% of Completion
Revenue	12,829.12	27,229.08	47.1%
GP	4,772.18	9,614.79	49.6%
Operating Profit	3,656.24	6,922.97	52.8%
EBIT	4,948.80	9,390.61	52.7%
EBT	4,064.65	7,540.68	53.9%
NP attributable to shareholders	2,769.86	5,177.62	53.5%

Source: Phillip Securities (HK) Research, Company Report

Table-4: Key Forecast and Target Price Revision

mn HKD		Old	New	% Change
Revenue	FY2019E	27,229.08	28,029.97	2.9%
	FY2020E	30,577.31	31,484.07	3.0%
	FY2021E	34,833.60	35,562.38	2.1%
GP	FY2019E	9,614.79	10,070.13	4.7%
	FY2020E	11,000.60	11,238.71	2.2%
	FY2021E	12,807.32	12,609.02	-1.5%
Operating Profit	FY2019E	6,922.97	7,325.98	5.8%
	FY2020E	8,032.71	8,241.81	2.6%
	FY2021E	9,481.22	9,230.85	-2.6%
NP attributable to shareholders	FY2019E	5,177.62	5,591.19	8.0%
	FY2020E	6,061.20	6,264.42	3.4%
	FY2021E	7,216.80	7,177.40	-0.5%
RI TP		5.81	5.83	0.3%

Source: Phillip Securities (HK) Research, Company Report

Financial Forecast and Valuation

We adjust the company's revenue in FY19/FY20/FY21 to be HKD 28.0/31.5/35.6 billion, representing increases of 13.96%/12.32%/12.95% YoY; net profit attributable to shareholders will be HKD 5.6/6.3/7.2 billion, representing increases of 25.05%/12.04%/14.57% YoY; corresponding EPSs are HKD 0.58/0.63/0.71. We adjust the TP of HKD 5.83, corresponding to FY19/FY20/FY21 10.06x/9.19x/8.21x PE with a +36.76% potential upside compared with CP of HKD 4.26 as of September 6, 2019, we maintain "BUY" investment rating.

Table-5: Comparable Peers

Co Name	Mkt Cap	EV	EV/TTM EBITDA	EV/EBITDA FY1	EV/EBITDA FY2	P/E	P/E FY1	P/E FY2	P/FCF	Dividend
CNY (2 securities)										
Median	9.45B	13.62B	10.9	10.2	8.42	22.74	17.89	14.8	31.38	1.39%
Mean	9.45B	13.62B	10.9	10.2	8.42	22.74	17.89	14.8	31.38	1.39%
600874.SH	9.93B	14.34B	--	--	--	22.41	--	--	--	1.41%
002672.SZ	8.97B	12.90B	10.9	10.2	8.42	23.06	17.89	14.8	31.38	1.38%
HKD (14 securities)										
Median	5.78B	14.47B	8.07	8.93	7.29	7.62	7.35	6.16	21.95	4.00%
Mean	17.23B	30.34B	8.63	9.68	8.21	13.71	8.65	7.23	21.95	4.63%
0270.HK	105.91B	109.65B	14.77	13.48	12.33	21	20.22	18.24	21.95	3.30%
371.HK	42.68B	104.49B	12	11.14	9.95	8.35	7.77	6.98	--	4.18%
257.HK	38.58B	78.59B	8.07	7.2	6.09	7.78	7.35	6.16	--	3.82%
1330.HK	11.82B	18.89B	--	18.1	14.17	12.74	9.51	7.41	--	3.24%
1257.HK	10.19B	16.53B	6.66	5.99	4.69	6.82	6.09	4.86	--	2.54%
855.HK	10.19B	25.59B	7.79	6.95	5.89	7.46	6.78	5.76	--	4.25%
1381.HK	8.71B	12.24B	8.5	8.13	6.8	10.48	9.57	8.08	--	1.29%
3989.HK	2.84B	12.40B	11.13	9.73	7.77	9.68	12.11	7.57	--	--
3768.HK	2.29B	5.10B	6.02	6.07	5.28	5.99	5.9	5.15	--	8.73%
1363.HK	2.15B	5.02B	4.5	--	--	3.24	--	--	--	--
6839.HK	2.12B	21.59B	12.19	10.07	9.09	5.11	4.39	4.16	--	9.56%
6136.HK	1.83B	11.47B	10.48	--	--	5.52	5.48	5.13	--	--
2281.HK	1.11B	1.49B	4.33	--	--	5.52	--	--	--	5.35%
1129.HK	766.34M	1.78B	5.8	--	--	82.26	--	--	--	--
SGD (2 securities)										
Median	4.35B	16.34B	9.07	8.94	8.21	6.18	5.96	5.25	0	3.83%
Mean	4.35B	16.34B	9.07	8.94	8.21	6.18	5.96	5.25	0	3.83%
U9E.SG	5.02B	12.11B	8.41	7.65	6.99	6.6	6.3	5.52	--	3.65%
BHK.SG	3.68B	20.57B	9.73	10.24	9.42	5.76	5.62	4.97	--	4.00%

Source: Phillip Securities (HK) Research, Bloomberg

Risk

1. Project progress fail expectations; 2. Industry policy; 3. Interest rate; 4. M&A fails expectations.

Financials

Table-6: Financial data

FYE DEC	FY17A	FY18A	FY19E	FY20E	FY21E
Valuation Ratios					
P/E	10.04	8.89	7.36	6.72	6.00
P/B	1.80	1.56	1.42	1.28	1.16
Dividend Yield	3.74%	4.34%	5.24%	5.74%	6.43%
Per Share Data in HKD					
EPS	0.42	0.48	0.58	0.63	0.71
DPS	0.16	0.18	0.22	0.24	0.27
BVPS	2.37	2.73	2.99	3.32	3.68
Growth & Margins (%)					
Growth					
Revenue	22.11%	16.06%	13.96%	12.32%	12.95%
Operating Profit	10.97%	44.09%	16.40%	12.50%	12.00%
Net Profit	20.90%	17.78%	24.48%	12.04%	14.57%
Margins					
Gross Margin	30.50%	35.68%	35.93%	35.70%	35.46%
Operating Profit Margin	20.61%	25.59%	26.14%	26.18%	25.96%
Net Profit Margin	20.95%	21.26%	23.23%	23.17%	23.50%
Key Ratios					
ROA	4.10%	3.94%	4.21%	4.36%	4.70%
ROE	19.94%	19.33%	20.55%	20.31%	20.52%
Income Statement in mn HKD					
Revenue	21,192.37	24,596.86	28,029.97	31,484.07	35,562.38
Gross Profit	6,464.52	8,775.94	10,070.13	11,238.71	12,609.02
EBIT	6,492.32	8,461.29	9,793.62	11,070.79	12,496.89
EBT	5,315.32	6,778.91	8,034.75	9,183.24	10,521.60
Net Profit	4,440.54	5,230.02	6,510.38	7,294.30	8,357.37
Net Profit for Owners	483.03	512.74	673.19	783.87	933.96

Source: Company, Phillip Securities (HK) Research
(Financial data as of September 6)

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

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