China Power Int`l Ltd (2380.HK)

Attractive valuation, cleaner power profile

Hong Kong | Electricity Supply | Company Report

7 March 2017

Investment Summary

-We are not optimistic about the FY2016 result, however the valuation is attractive.

-The national total electricity consumption has grown steadily in 2016, if the steady growth continues, we reckon the firm has still-favorable long term prospects.

-It is expected that China coal price correction continues, and high coal price has less impact on the firm because of the firm`s cleaner profile.

Company Overview

China Power International Development Limited mainly engaged in generation and sales of electricity in Mainland China, including investment, development, operation and management of coal-fired power, hydropower, wind power and photovoltaic power plants. Acorrding to the 1H2016 interim result, the total electricity sold was 32,550,127MWh, representing an increase of 15.35% as compared with the corresponding period last year. The performance of the hydropower business was favorable, benefited from the abundant rainfall and taking full advantage of optimizing the highly effective cascade watershed management to increase power generation. The net profit attributable to equity holders of the Company was RMB1,926.08 million, representing a YoY decrease of 29.04%. However, save for the before tax one-off gain on disposal of partial interest in Shanghai Power in the corresponding period last year, the Group`s net profit increased by approximately 1.32% as compared with the corresponding period last year.

Although the 2016 first half result was acceptable for shareholders, we are 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.

However, the stock is trading at approximate 7.2x FY2016Est PE and 0.7x Price to Book Ratio, we believe most unfavorable information basically priced in on the stock price. In last year, the stock had underperformed by around 32% compared with the Hang Seng Index, which the valuation might already become appealing.

Moreover, the high coal price has less impact on the firm compared with its peers since it has a cleaner profile. Because the firm`s attributable installed capacity for clean energy accounting for around 20% of the Group`s total attributable installed capacity.

Accumulate

CMP: HKD 3.04
(Closing price as at 3 MAR 2017)
TARGET: HKD 3.61 (+18.75%)

COMPANY DATA

O/S SHARES (MN) :	7,355
MARKET CAP (HKDMN) :	22,212
52 - WK HI/LO (HKD):	4.15/ 2.69

SHARE HOLDING PATTERN, %

State Power Investment Corporation	55.61

PRICE PERFORMANCE, %

	1M	3M	1Y
China Power	+8.96	+5.92	-16.09
HSI	+2.58	+4.84	+16.91

PRICE VS. HSI



Source: Phillip Securities (HK) Research

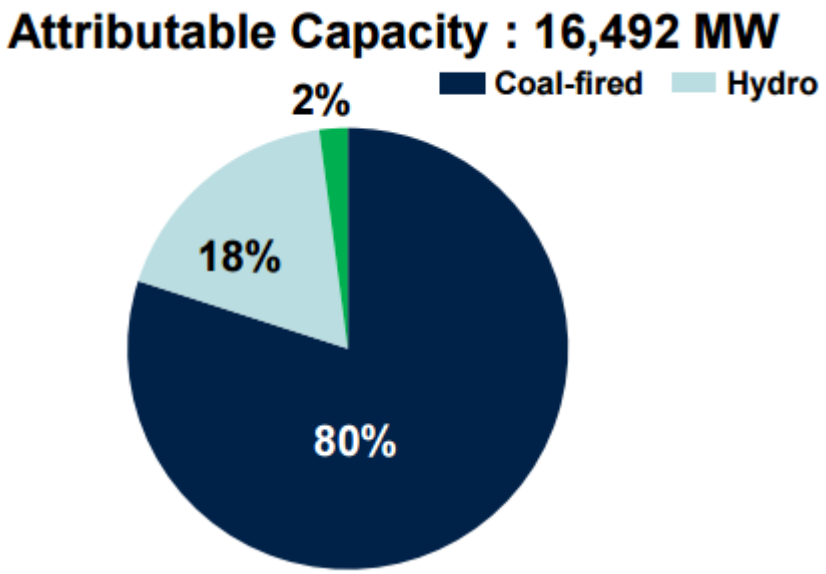
KEY FINANCIALS

CNY mn	FY14	FY15	FY16E	FY17E
EPS, CNY	0.42	0.58	0.37	0.29
PE, x	7.49	6.47	7.10	9.16
BVPS, CNY	3.17	3.71	3.87	4.01
P/BV, x	0.99	1.01	0.70	0.68
ROE, %	13.73	16.87	10.07	8.13
Debt/Equity (%)	208.33	156.25	-	-

Source: Company reports, Phillip Securities Est.

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The graph in below shows the attributable installed capacity respective ratio of contribution to the total capacity:



Source: Company Report, Phillip Securities (HK) Research

According to the 2016 1H result, the attributable installed capacity of coal-fired power was 13,187MW, representing approximately 79.96% of the total attributable installed capacity, and the attributable installed capacity of renewable energy including hydropower, wind power and photovoltaic power was 3,305MW, representing approximately 20.04% of the total attributable installed capacity. In 2015, the Group`s attributable installed capacity for clean energy amounted to 3,119MW, accounting for 19.19% of the Group`s total attributable installed capacity. From the 2016 1H result, the net profits respective ratio of contribution to the total net profit are as follows: coal-fired power was approximately RMB1,265.53 million (48.5%,); hydropower was approximately RMB1,318.07 million (50.5%,); and wind power and photovoltaic power was approximately RMB26.7 million (1.0%). From the figures above, we can see that the coal-power business has become slightly less important for the firm.

In addition, as the firm is one of the largest power generators in China. It is hard to ignore that the group is in the monopoly industry, 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. Thereby, the group still has favorable long-term prospects.

Peer Comparison

Ticker	P/E	P/B	Dvd Yld(%)	ROE(%)
2380 HK	7.20	0.70	5.89	10.07
902 HK	7.06	0.80	5.88	10.94
836 HK	7.57	0.90	5.71	12.13
991 HK	-	0.67	-	-3.23
1071 HK	8.26	0.67	4.94	9.51
6 HK	19.52	1.19	3.98	6.08
2 HK	14.17	1.84	3.53	13.3

Source: Bloomberg, Phillip Securities (HK) Research

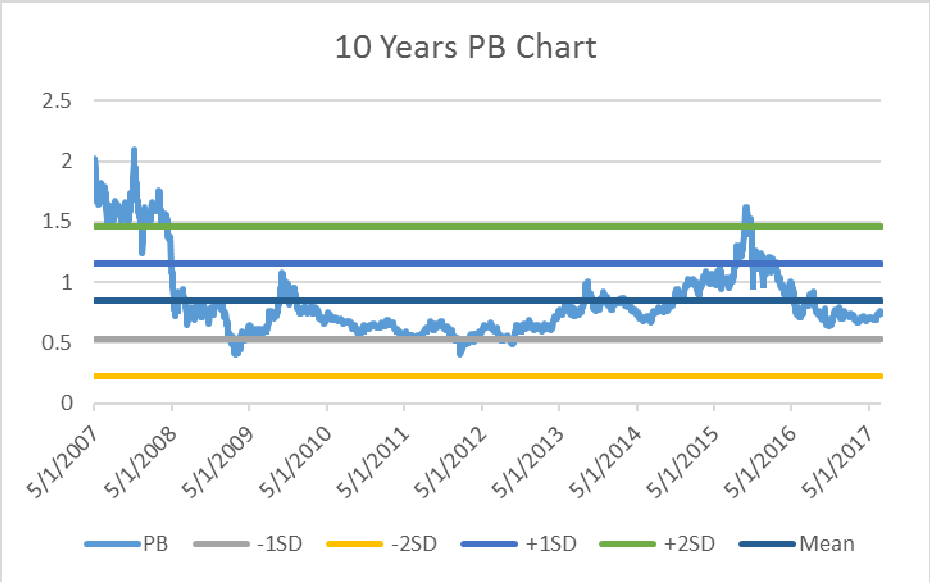
The table in above shows the peer comparison of the group.

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 similar to its Chinese peers such as Huaneng Power(902 HK), Huadian Power(1071 HK),and China Resources Power(836 HK).

The Valuation is attractive

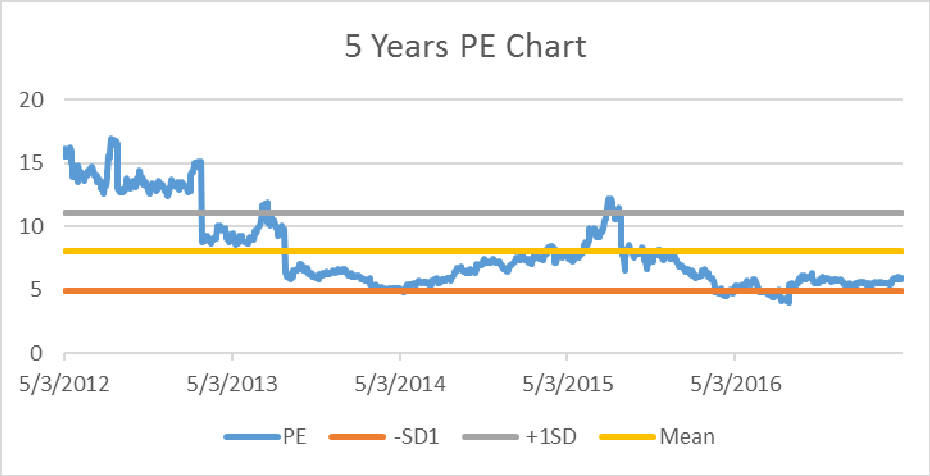
First of all, to examine whether the stock is undervalued, historical PB and PE band could be useful.

The chart below shows 10 years of PB ratio of the stock, the statistic started on 24/3/2007, with 2 standard deviations.



Source: Bloomberg, Phillip Securities (HK) Research

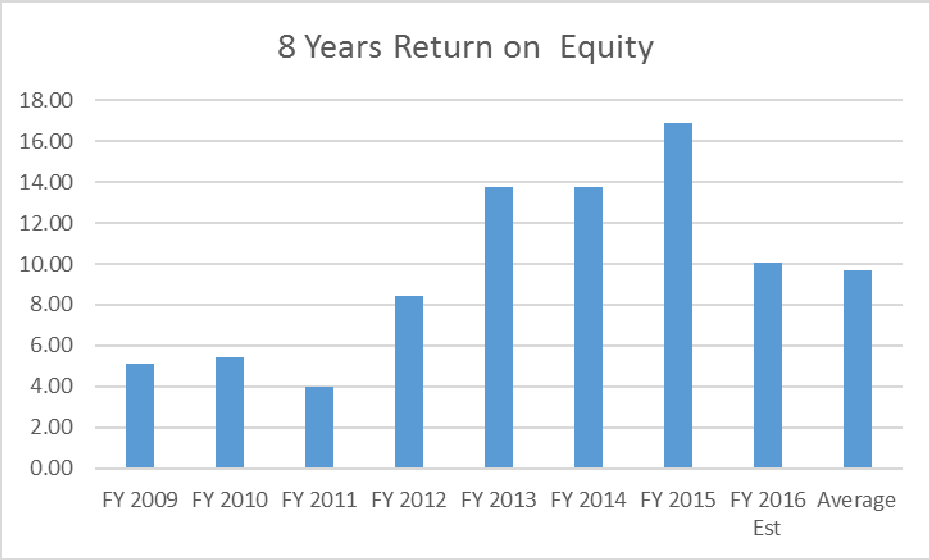
From the chart above, we can see that the PB valuation is lower than the 10 years average. Approximately, the average 10 years PB ratio is 0.84x, one standard deviation below is 0.54x, and the stock trades below the 10 years average but above 1 standard deviation.



Source: Bloomberg, Phillip Securities (HK) Research

The table above shows the 5 years PE band, the statistic started on 5/3/2012, with 1 standard deviation. The average 5 years PE ratio is approximately 8x, one standard deviation below is 4.92x, and the stock trades below the 10 years average but above 1 standard deviation. Overall, in term of the PE/PB ratio, the valuation is appealing but not extremely attractive.

The Return on Equity ratio is also crucial, which can provide more information regarding the profitability of the group.



Source: Bloomberg, Phillip Securities (HK) Research

According to the bar chart in above, the ROE for 2016 expected to be 10.07%, which is still higher than the 8 years average ROE of 9.66%, indicating that the profitability is still acceptable for the period, and the stock trades at only around 0.7x PB ratio currently. This could indicated the stock has possibly become undervalued.

Moreover, to see whether China 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%, datas collected from 31th Dec 1995 to 31th DEC 2016. We used the 10 years China government bond yield of 3.42% as the risk free rate, and the historical Beta

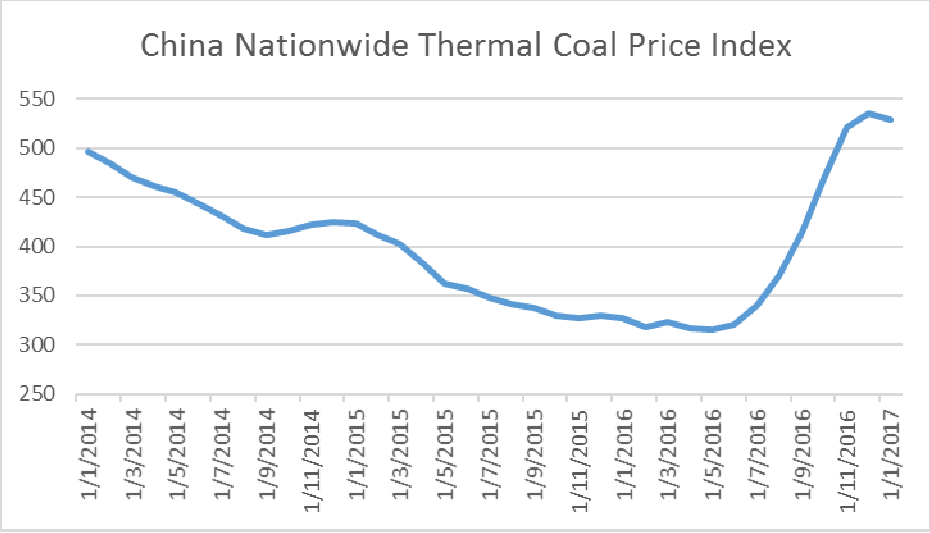
of the stock is 0.94. From that, we calculated that the required return of the stock is 6.99%. Our prudently forecasted dividend per share for next year is 0.13 RMB per share. Basic on the 8 years average ROE figure, and the dividend payout ratio will stays the same as 40.6%, we speculated the dividend growth rate is 3.92% under normal situation. As a result, we calculated the intrinsic value of RMB 4.23 per share for the normal situation, For the worst situation, the dividend growth rate is only 2.92%, which is significantly lower than the country`s historical GDP growth rate, the intrinsic value is still RMB 3.19 per share. Which also around 15% higher than its current price. Therefore, the share is trading at below intrinsic value, indicating that it is reasonable to believe that the stock is undervalued.

China electric consumption expected to grow steadily

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.

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 rose to 528.54 per tonne in the first month of 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 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 surge would possibly ended in recent time, and at least a price correction is expected, it is beneficial to the firm`s fuel cost reduction. Moreover, the attributable installed capacity of renewable energy including hydropower, wind power and photovoltaic power was 3,305MW, representing approximately 20.04% of the total attributable installed capacity, the high coal price has a less significant impact on the firm compared its peers. 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 Power International Development Limited`s target price is therefore $3.61, with Accumulate rating assigned, represents 0.83x FY16 P/B and 0.80x FY17 P/B. (Closing price as at 3 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.

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-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
Valuation Ratios					
Price Earnings Ratio (P/E)	5.39	7.49	6.47	7.10	9.16
Price to Book Ratio	0.75	0.99	1.01	0.70	0.68
Per share Data(RMB)					
Basic Earnings per Share	0.40	0.42	0.58	0.37	0.29
Book Value per Share	2.88	3.17	3.71	3.87	4.01
Dividends per Share	0.16	0.17	0.23	0.16	0.13
Revenue Growth YoY	-0.38	4.66	-8.08	-11.99	2.01
Growth & Margins(%)					
Revenue Growth	7.60	8.61	-1.23	-2.05	0.85
EPS Growth	81.82	5.00	38.10	-36.21	-21.62
Net Income Growth	93.87	20.79	50.01	-36.21	-21.62
Operating Profit Margin	27.20	28.39	38.45	28.59	23.11
Net Profit Margin	12.16	13.53	20.54	14.41	11.24
Key Ratios					
ROE	13.73	13.73	16.87	10.07	8.13
ROA	3.12	3.49	4.94	4.12	3.08
Income Statement(RMB:mn)					
Revenue	18,826.7	20,447.2	20,196.7	19,782.0	19,950.8
Operating Income or Losses	5,121.0	5,805.4	7,766.4	5,655.2	4,610.5
Pre-Tax Income	4,234.1	4,302.7	6,553.0	4,866.3	3,889.8
Net Income/Net Profit (Losses)	2,289.9	2,765.9	4,149.0	2,903.7	2,307.0

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

(Financial figures as at 3 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 ± 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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