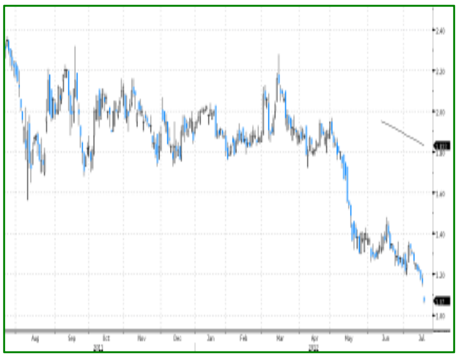
農銀國際
ABC INTERNATIONAL
ABCI SECURITIES COMPANY LIMITED

Huaneng Renewables (958) - Downgrade to HOLD

Share Data

Price (17/07/2012)	HK$1.16
12 mth target price	HK$1.21
52 wk high/low (HK$)	2.45/1.14
Stock code	958
Issued shares (mn)	8,446.9
H-shares	2,911.6
Domestic shares	5,535.3
H-share Market cap (HK$ mn)	3,377.44
H-share free-float	69.41%
15-day avg vol (mn)	4.20
Auditors	KPMG
Controlling shareholder:	
Huaneng Group	65.5%



ABCI Securities Company Limited and/or its associates will seek to do business with Huaneng Renewables Corporation Limited. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision. Investors should obtain relevant and specific professional advice appropriate to his/her/its personal circumstances and investment objectives before making any investment decision. Investor should also carefully consider relevant risk factors. If an investor has any questions about anything contained in this research report please consult ABCI Securities Company Limited or his/her/its professional advisors.

Report date: 18 Jul, 2012

Analyst:
Lisa Lee (Lisalee@abci.com.hk)
Tel: (852) 21478809

Huaneng Renewables (958) announced profit warning due to worsening grid curtailment issue in 1H2012, extended small wind phenomenon and diminishing income from CERs. In our view, the three major reasons which caused worse-than-expected results of the group were factors affecting the industry as a whole rather than caused by specific business risks associated with the group. Since wind resources and CERs prices are uncontrollable factors, the pace of grid investment and construction becomes an essential signal for a turnaround in the industry going forward.

Grid curtailment issue: After discussing with managements of the major wind farm operators, we realized that the grid curtailment problem was becoming more severe in 1H2012 compared to 2H2011. Wind curtailment rate in regions such as Inner Mongolia, Gansu and Liaoning were over 25% in 1H2012 compared to 17% in 2H2011. In view of the grid curtailment problem, the group has decided not to have any newly installed capacity built in Inner Mongolia in 2012 and instead focusing on development in Yunnan, Shanxi, Guangdong and Guizhou, which we believed could help alleviating the wind curtailment problem and allowing the group to outperform its peers. However, as consolidated installed capacity in these newly developed regions only accounted for less than 20% of total installed capacity of the group by the end of 2011 as compared to 56% of installed capacity in Inner Mongolia and Liaoning, the worse-than-expected grid curtailment issues remained an overhang on the group, as well as the whole wind power sector. According to the group, consolidated gross power generation in Inner Mongolia, Liaoning and Xinjiang of the group dropped 37.0%YoY, 6.1%YoY and 2.3%YoY to 819GWh, 932GWh and 154GWh respectively. Therefore, despite a 40%YoY increase in installed capacity in 2011, total gross power generation increased by only 7%YoY in 1H2012.

How long would it last? Grid curtailment issue was a result of faster expansion of installed capacity than grid investment over the past few years. Although there were policies in speeding up the construction of ultra high voltage grid lines in China, the long construction period would mean that grid curtailments can only be solved in at least 1-2year time. In addition, the issue is further complicated by grid investment incentive of grid companies. The relatively higher on-grid tariff of wind power than to coal-fired power has reduced the incentive for grid companies to invest especially when electricity consumption is slowing down due to slower economic growth. The grid curtailment issues may last for longer than 1-2 years unless we see a high enough economic growth and electricity consumption which can motivate a faster investment in grid constructions. Even though the “Quotation System” which was expected to be announced by the end of this year may help easing the problem but implementation and enforcement of the policy can take time.

Risk on fairness on connecting to grid: We observed that Huade Wind Power in Inner Mongolia operated by Huaneng Power (902), one of the listed subsidiaries of the group’s parent, posted 52.8%YoY increase gross power generation to 110GWh. The substantial contrast in change of power output may indicate a sign of unfairness in terms of grid connection priority within the wind power sector.

Longer-than-expected small wind phenomenon: Apart from the grid curtailment issues, the small wind phenomenon occurred in 2H2011 extended till 1Q2012. Wind resources are natural risks to the industry which have very low visibility and are uncontrollable. However, a higher amount of wind resources is expected in coming years as the possibility of an increase in wind resources seems to be more likely to occur after a “small wind year”. Nevertheless, the extent of increase of utilization hours due to higher wind resources are limited by the grid curtailment issues stated above.

Diminishing income from CERs: CER sales agreements signed between the group and buyers had fixed unit price of approx. Eur10 and valid till Dec 2012. However, as price of CERs dropped from Eur10 in 2011 to as low as Eur3.08 up to date, we believe the group were not able to collect the full amount of CERs income as stated in the contracts, causing a diminishing income from CERs, which we had already factored in our model previously. We expect the continue downtrend in the CERs price are a results of rapid development of green energy companies which lead to a larger supply in CERs and the trend is unlikely to change in a short period of time.

Valuation: The major reasons that caused our downgrade are the worsening grid curtailment issues and longer-than-expected small wind phenomenon for which we have adjusted our weighted average utilization hours assumptions from 2,050 hours to 1,800 hours in 2012. NP of the group is expected to drop below Rmb337mn in 1H2012. However, due to expectation on better wind resources in 2H2012 and reflection of newly installed capacity in regions with no curtailment issues, we expect the group to post better 2H2012 results on HoH basis. We revised down our est. 2012 EPS by 42.8% to Rmb0.0959, down 20.9%YoY and based on est 2012 ROAE of 7.0%, we give it a 12 month TP of HK$1.21, representing 10.2 x 2012 PE and 0.7x 2012 PB. We downgrade our rating from “BUY” to “HOLD”.

Share price risks: After China Windpower (182), the group is the second HK-listed wind power company announced a profit warning within the sector. Further bad news might be released from peers in the short term, leading to high share price volatility for the whole sector.

Financial Summary

FY ended Dec 31	2010	2011	2012F	2013F
Revenue (Rmb mn)	1,768.5	3,195.9	3,882.9	5,099.4
Change (YoY)	*92.6%*	*80.7%*	*21.5%*	31.3%
Net profit (Rmb mn)	528.3	1,023.0	809.7	1,235.6
Change (YoY)	*99.8%*	*93.7%*	*-20.9%*	52.6%
FD EPS (Rmb)	0.0911	0.1211	0.0959	0.1463
Change (YoY)	*99.8%*	*32.9%*	*-20.9%*	52.6%
PER (x)	-	7.78	9.83	6.44
NBV (Rmb/share)	0.9110	1.3415	1.3999	1.5318
PB (x)	-	0.70	0.67	0.61
ROAA	2.06%	2.41%	1.49%	2.04%
ROAE	13.43%	12.31%	6.99%	9.98%

@(HK$0.8121/Rmb)
Source: Huaneng Renewables (historical figures only), F: ABCI Securities estimates

Disclosures

Analyst Certification

I, Lee Oi-yee, Lisa , being the person primarily responsible for the content of this research report, in whole or in part, hereby certify that all of the views expressed in this report accurately reflect my personal view about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

ABCI Securities Company Limited and/or its member companies ("ABCI") may pursue financial interests to the companies mentioned in the report.

Disclaimer

This report is for our clients only and is for distribution only under such circumstances as may be permitted by applicable law. It has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient. It is published solely for informational purposes and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments. No representation or warranty, either expresses or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein. This report should not be regarded by recipients as a substitute for the exercise of their own judgment. Any opinions expressed in this report are subject to change without notice and may differ or be contrary to opinions expressed by other business areas as a result of using different assumptions and criteria. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. The analyst(s) responsible for the preparation of this report may interact with trading desk personnel, sales personnel and other constituencies for the purpose of gathering, synthesizing and interpreting market information. ABCI Securities Company Limited is under no obligation to update or keep current the information contained herein. ABCI Securities Company Limited relies on information barriers to control the flow of information contained in one or more areas within ABCI Securities Company Limited, into other areas, units, Groups or affiliates of ABCI Securities Company Limited. ABCI Securities Company Limited will not pay any research analyst any bonus, salary or other form of compensation that is based upon a specific investment banking transaction. The analysts' compensation shall be based upon several factors. Chiefly among such factors is the quality of the research and financial advice provided to our customers and the impact that the analysts' research has on the success of the Company's overall business. The final compensation of the analyst who prepared this report is determined exclusively by research management and senior management of ABCI Securities Company Limited. The securities described herein may not be eligible for sale in all jurisdictions or to certain categories of investors. The price and value of the investments referred to in this research and the income from them may fluctuate. Past performance is not necessarily indicative of future results. Foreign currency rates of exchange may adversely affect the value, price or income of any security or related instrument mentioned in this report. For investment advice, trade execution or other enquiries, clients should contact their local sales representative. Neither ABCI Securities Company Limited nor any of its affiliates, directors, employees or agents accepts any liability for any loss or damage arising out of the use of all or any part of this report. Additional information will be made available upon request.

Office address : **ABCI Securities Company Limited, 13/F Fairmont House, 8 Cotton Tree Drive, Central, Hong Kong.**

Tel : **(852) 2868 2183**