August 28, 2015
Company Report
Rating: BUY
TP: HK$ 7.70

Share price (HK$)	5.35
Est. share price return	43.93%
Est. dividend yield	1.49%
Est. total return	45.42%

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Key Data

Market share (HK$mn)	46,633
3-mth avg. daily turnover (HK$ mn)	120
52-week high/low (HK$)	7.31/4.13
Issued shares (mn)	8,707
Major shareholder(s) (%):	
Beijing Enterprises Hld	43.92

Source(s): Company, Bloomberg, ABCI Securities

FY14 Revenue breakdown (%)

Wastewater	**87.75**
Operation	36.41
Construction	51.34
Water distribution	9.10
Others	3.14

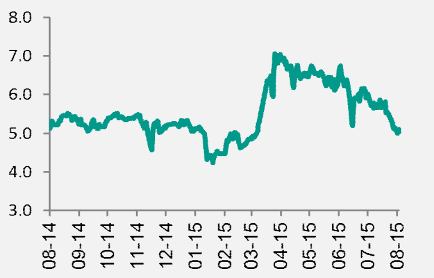
Source(s): Company, ABCI Securities

Share performance (%)

	Absolute	Relative*
1-mth	-6.79%	4.08%
3-mth	-18.32%	2.05%
6-mth	10.90%	23.21%

*Relative to HSI
Source(s): Bloomberg, ABCI Securities

1-Year stock performance (HK$)



Source(s): Bloomberg, ABCI Securities

Beijing Enterprises Water (371 HK)

1H15 review: strong fundamentals to continue

- Beijing Enterprises Water (BEW) announced 1H15 results with net income rising by 46%YoY, which accounts for 46% of the Bloomberg full-year estimate and in line with the Group's historical run rate of 45%
- Wastewater and water distribution capacity growth were slower than expected; however, tariff growth of 13%YoY was a bright spot
- We expect the Group's wastewater and water distribution capacities to expand by 23% YoY and 30%YoY in 2015E and boost earnings by 28%YoY
- We reiterate our BUY rating. Our TP HK$7.70 is derived from a 11% WACC and represents 29x/24x FY15E/16E P/E and 3.8x/3.3x FY15E/16E P/B

Possible capacity growth of 23%/30%YoY in wastewater/water distribution in 2015E. BEW recorded a slower-than-expected wastewater and water distribution capacity growth in 1H15. Nonetheless, we believe the Group would still achieve a robust growth in 2015, as management said a capacity of 1.8mt/day (wastewater and water distribution) has completed construction and another 2.6mt/day capacity is now under construction. Together with potential new M&A projects this year, the Group is confident of achieving an additional capacity of 3mt/day by end-2015.

Uptrend in China wastewater tariff should continue – a big plus to BEW. In 1H15, BEW recorded a 13%YoY growth in wastewater tariff. We believe the rise has been driven by strong demand for wastewater treatment in urban areas and the increasing stringent nationwide wastewater quality standard, which in turn urged local governments to improve wastewater treatment. Amid rising concern over water pollution and increasing urbanization in China, nationwide wastewater tariffs grew at a 9% CAGR during 2000-15. Water tariffs should maintain its uptrend going forward and provide strong support to BEW's margins.

High net gearing ratio may trigger fundraising activities. Although management expressed the Group has no new placement plan, its high net gearing ratio (1H15 at 119%) may hinder BEW's rapid expansion in wastewater capacity going forward. In addition, the Group revealed its planned capex for 2015 would be ~HK$8bn. With HK$ 4.6 bn of cash on hand by 1H15, BEW may carry out fundraising activity in the future.

Reiterate BUY with TP at HK$ 7.70. 1H15 results was in line with expectations and we remain positive on BEW's future earnings growth. Our TP of HK$ 7.70 unchanged represents 29x/24x 2015E/16E P/E and 3.8x/3.3x 2015E/16E P/B. We estimate a 2014-2017E EPS CAGR of 23%, equivalent to around 1.0x 2016E PEG. Reiterate **BUY.**

Risks: (1) Default risk; (2) High net gearing ratio may prompt fundraising activities; (3) Policy risks. (4) Slower-than-expected M&A and construction progress.

Results and Valuation

FY ended Dec 31	2013A	2014A	2015E	2016E	2017E
Revenue (RMB mn)	6,406	8,926	11,692	14,947	18,323
Chg (%,YoY)	71.9	39.3	31.0	27.8	22.6
Net Income (RMB mn)	1,084	1,794	2,299	2,826	3,358
EBITDA (RMB mn)	1,973	3,515	4,081	5,350	6,689
Chg (%,YoY)	66.0	78.1	16.1	31.1	25.0
EPS (RMB)	0.140	0.208	0.266	0.327	0.388
Chg (%,YoY)	28.7	48.5	28.1	22.9	18.8
BVPS (RMB)	1.715	1.826	2.011	2.310	2.581
Chg (%,YoY)	39.9	6.5	10.1	14.8	11.8
P/E (x)	55.08	37.93	28.95	23.55	19.82
P/B (x)	4.49	4.22	3.83	3.33	2.98
ROE (%)	8.15	11.37	13.23	14.16	15.05
ROA (%)	2.45	3.47	3.56	3.51	3.48
DPS(RMB)	0.055	0.079	0.080	0.098	0.117
Yield (%)	0.71	1.02	1.04	1.27	1.51
Net gearing* (%)	84.2	92.3	153.2	193.8	230.6

*Net gearing=Net debt/Total equity
Source(s): Bloomberg, ABCI Securities estimates

Beijing Enterprises Water (BEW) announced its 1H15 results on August 27. Net income was HK$ 1,160 mn (+63% YoY); excluding non-core fair value gain on derivative financial instruments, net income was HK$ 1,045 (+46% YoY), the figure represents 46% of Bloomberg's full-year estimate and 45% of our 2015E estimate, and is in line with the Group's historical run rate of 45%.

1H15 results highlight:

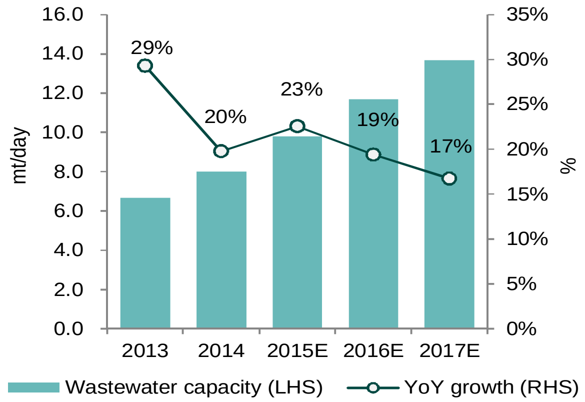
- **Wastewater/water distribution capacity growth of 9%/3%YoY is slower than expected.** Management revealed that increasing competition has slowed M&A progress and suppressed capacity growth in 1H15. However, BEW said the Group had accelerated construction progress and completed the construction of 1.8mt/day capacity (wastewater and water distribution) and is confident of adding a capacity of 3mt/day (+26%YoY) by end-2015.
- **Wastewater tariff growth of 13%YoY as the bright spot.** According to management, the higher water tariff has been mainly driven by the increasingly stringent standard of nationwide wastewater quality that urged local governments to improve wastewater treatment.
- **Net gearing ratio of 119% may prompt fundraising concern.** The Group said the high gearing was resulted from increasing consideration of M&A and construction expenses for new projects. The Group said the ratio would not exceed130%-150%.

Reiterate BUY; TP at HK$7.70

BEW's 1H15 net income achieved 45% of our full-year estimate, which is in line with its historical run rate of 45%. We believe its wastewater and water distribution capacity growth should remain robust going forward as the Chinese government is likely to announce more supportive policies in near future.

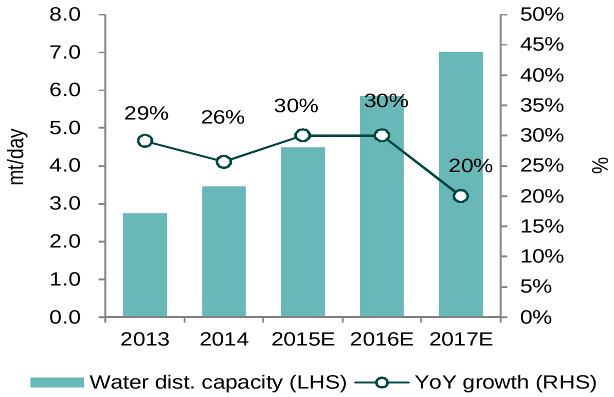
We keep our TP HK$7.70 unchanged as BEW's 1H15 results were in line with our estimates. Our TP is equivalent to 29x/24x 2015/16E P/E and 3.8x/3.3x 2015/16E P/B. Robust growth in wastewater and water distribution capacity should continue to support its earnings growth, while the rising nationwide water tariff should provide solid support for margins. We expect BEW to deliver a 23% EPS CAGR during 2014-2017E, equivalent to ~1.0x 2016E PEG.

Exhibit 1: BEW's wastewater capacity outlook



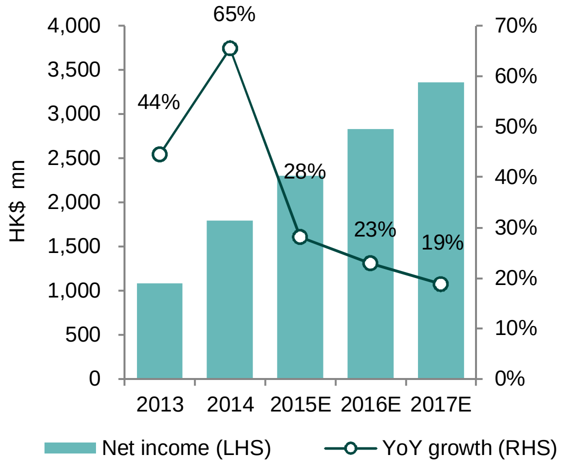
Source(s): Company data, ABCI Securities estimates

Exhibit 2: BEW's water distribution capacity outlook



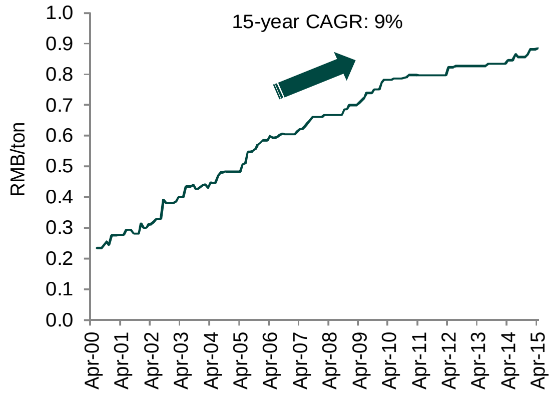
Source(s): Company data, ABCI Securities estimates

Exhibit 3: BEW's net income outlook



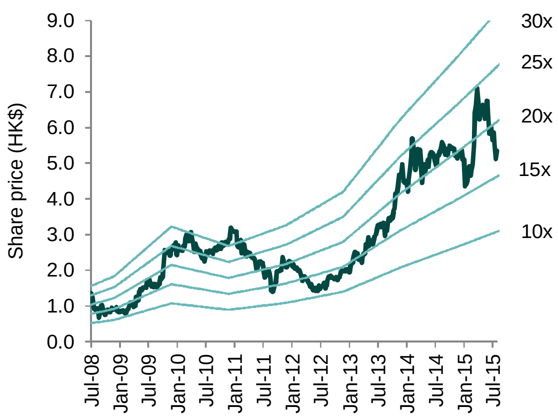
Source(s): Company data, ABCI Securities estimates

Exhibit 4: China's wastewater tariff maintains an uptrend



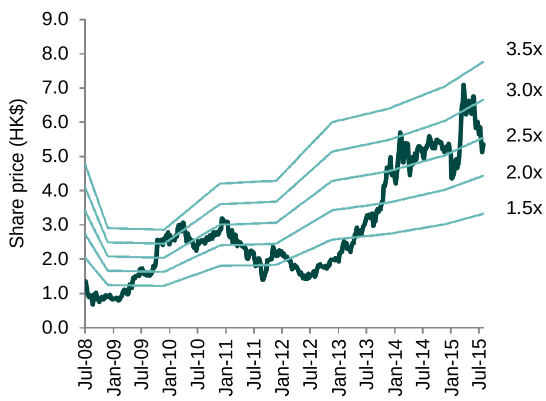
Source(s): Company data, ABCI Securities estimates

Exhibit 5: BEW's fwd PE chart



Source(s): Bloomberg, ABCI Securities estimates

Exhibit 6: BEW's fwd PB chart



Source(s): Bloomberg, ABCI Securities estimates

Consolidated income statement (2013A-2017E)

FY Ended Dec 31 (HK$ mn)	2013A	2014A	2015E	2016E	2017E
Revenue	**6,406**	**8,926**	**11,692**	**14,947**	**18,323**
Sewage and reclaimed water	5,905	7,833	10,249	13,061	16,005
Water distribution	384	813	1,121	1,515	1,892
Other	118	281	323	371	427
COGS	**-3,901**	**-5,430**	**-7,034**	**-8,906**	**-10,838**
Gross profit	**2,506**	**3,496**	**4,658**	**6,042**	**7,486**
SG&A	-775	-1,066	-1,169	-1,495	-1,832
Net financial income (cost)	-354	-639	-588	-996	-1,448
Other income and gains	120	876	292	374	458
Pre-tax profit	**1,497**	**2,667**	**3,193**	**3,925**	**4,663**
Income tax	-352	-594	-639	-785	-933
Net profit	**1,145**	**2,073**	**2,554**	**3,140**	**3,731**
Profit attributable to:					
Minority interests	-61	-279	-255	-314	-373
Equity shareholders of the Company	**1,084**	**1,794**	**2,299**	**2,826**	**3,358**
Basic EPS (HK$)	**0.140**	**0.208**	**0.266**	**0.327**	**0.388**
DPS (HK$)	**0.055**	**0.079**	**0.080**	**0.098**	**0.117**

Source(s): Company, ABCI Securities estimates

Consolidated balance sheet (2013A-2017E)

As of Dec 31 (HK$ mn)	2013A	2014A	2015E	2016E	2017E
Current assets	**15,212**	**15,078**	**16,647**	**17,906**	**19,019**
Cash and equivalent	5,513	6,091	6,610	5,077	3,293
Pledged and restricted bank deposits	57	304	0	0	0
Trade and bill receivables	2,038	2,595	3,524	4,505	5,522
Other receivables and prepayments	6,431	5,910	6,407	8,190	10,040
Inventories	55	58	106	134	163
Other current assets	1,118	120	0	0	0
Non-current assets	**28,974**	**36,563**	**47,875**	**62,644**	**77,332**
Property, plant and equipment	379	1,243	2,102	2,958	3,812
Lease prepayment	0	0	0	0	0
Intangible assets	2,539	2,553	3,494	4,667	6,078
Investment in JV and associates	3,025	3,109	3,851	4,780	5,901
Other receivables and deposits	15,006	20,293	26,105	33,151	40,458
Other non-current assets	8,027	9,364	12,323	17,087	21,084
Total assets	**44,187**	**51,641**	**64,522**	**80,550**	**96,351**
Current liabilities	**11,651**	**11,419**	**16,183**	**20,856**	**25,796**
Trade and bill payables	2,755	3,564	4,818	6,100	7,423
Other payables	4,908	3,910	4,818	6,100	7,423
Short term borrowings	3,980	3,945	6,547	8,656	10,949
Other current liabilities	7	0	0	0	0
Non-current liabilities	**16,611**	**21,133**	**27,396**	**35,859**	**43,998**
Deferred tax liabilities	562	930	700	750	200
Long-term borrowings	12,780	17,022	26,696	35,109	43,798
Other non-current liabilities	3,269	3,182	0	0	0
Total liabilities	**28,262**	**32,552**	**43,579**	**56,715**	**69,793**
Minority interests	**-2,627**	**-3,304**	**-3,560**	**-3,874**	**-4,247**
Shareholders' equities	**13,298**	**15,784**	**17,383**	**19,961**	**22,312**

Source(s): Company, ABCI Securities estimates

Consolidated cash flow statement (2013A-2017E)

FY ended Dec 31 (HK$ mn)	2013A	2014A	2015E	2016E	2017E
Profit before tax	**1,497**	**2,667**	**3,193**	**3,925**	**4,663**
Change in depreciation and amortization	122	209	299	429	578
Change in working capital	-2,653	-2,732	-9,072	-9,504	-9,869
Net finanical cost (income)	363	668	588	996	1,448
Income tax paid	-177	-277	-594	-639	-785
Net interest received	0	0	0	0	0
Others	-88	-271	-175	-224	-275
CF Operating	**-936**	**264**	**-5,761**	**-5,017**	**-4,240**
Capex	-105	-683	-1,291	-1,479	-1,672
Increase in intangible assets	-19	-51	-937	-1,169	-1,407
Others	-2,734	-1,000	-1,886	-2,288	-2,701
CF Investing	**-2,857**	**-1,734**	**-4,114**	**-4,936**	**-5,780**
Net Capital raise	2,297	0	-6	0	0
Net debt financing	3,726	3,677	12,276	10,523	10,982
Dividend payout	0	-10	-690	-848	-1,007
Interest paid	-789	-1,105	-1,084	-1,153	-1,637
Others	191	-366	0	0	0
CF Financing	**5,425**	**2,196**	**10,496**	**8,522**	**8,338**
Net change in cash	**1,632**	**726**	**621**	**-1,432**	**-1,682**
Cash at the beginning	3,640	5,366	6,091	6,610	5,077
Adjustment (Time deposit & FX effect)	241	-1	-102	-102	-102
Cash at the end	**5,513**	**6,091**	**6,610**	**5,077**	**3,293**

Source(s): Company, ABCI Securities estimates

Key Ratio (2013A-2017E)

FY ended Dec 31 (HK$ mn)	2013A	2014A	2015E	2016E	2017E
Sales mixed (%)					
Sewage and reclaimed water	92.18	87.75	87.65	87.38	87.35
Water distribution	5.99	9.10	9.59	10.14	10.32
Other	1.83	3.15	2.76	2.48	2.33
Total	**100**	**100**	**100**	**100**	**100**
Profit & loss ratios (%)					
Gross margin	39.11	39.17	39.84	40.42	40.85
Operating profit margin	27.21	33.92	30.84	31.42	31.85
Pre-tax margin	23.37	29.88	27.31	26.26	25.45
Net profit margin	17.88	23.23	21.85	21.01	20.36
Selling & administrative expenses/revenue	12.09	11.94	10.00	10.00	10.00
Effective tax rate	23.50	22.27	20.00	20.00	20.00
Growth (%)					
Revenue	71.88	39.33	30.99	27.84	22.59
Gross profit	74.36	39.53	33.24	29.71	23.90
Operating profit	63.85	73.68	19.09	30.25	24.28
Net profit	32.09	81.01	23.21	22.91	18.82
Balance sheet ratios					
Current ratio (x)	1.31	1.32	1.03	0.86	0.74
Quick ratio (x)	0.65	0.79	0.63	0.46	0.34
Cash ratio (x)	0.48	0.56	0.41	0.24	0.13
Trade and bill receivables days	116.11	106.12	110.00	110.00	110.00
Trade and bill payables turnover days	257.82	239.56	250.00	250.00	250.00
Inventory turnover days	5.18	3.88	5.50	5.50	5.50
Total debt / equity ratio (%)	126.04	132.83	191.24	219.25	245.38
Net debt / equity ratio (%)	84.15	92.32	153.21	193.82	230.61
Returns (%)					
ROAA	2.9	3.7	4.0	3.9	3.8
ROAE	10.0	12.3	13.9	15.1	15.9
Payout ratio	39.28	37.85	30.00	30.00	30.00

Source(s): Company, ABCI Securities estimates

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Definition of equity rating

Rating	Definition
Buy	Stock return Ó Market return rate
Hold	Market return ï 6% Ò Stock return < Market return rate
Sell	Stock return < Market return ï 6%

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months
Market return: 5-year average market return rate from 2010-2014
Time horizon of share price target: 12-month

Definition of share price risk

Rating	Definition
Very high	2.6 Ò 180 day volatility/180 day benchmark index volatility
High	1.5 Ò 180 day volatility/180 day benchmark index volatility < 2.6
Medium	1.0 Ò 180 day volatility/180 day benchmark index volatility < 1.5
Low	180 day volatility/180 day benchmark index volatility < 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index.
Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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