

China Water Affairs Group

FY19 results

Extending the earnings growth record

Utilities

2 July 2019

Price **HK\$7.69**
Market cap **HK\$12,372m**

Net debt (HK\$bn) at 31 March 2019 10.3

Shares in issue 1,608.9m

Free float 66%

Code 855

Primary exchange HK

Secondary exchange N/A

Share price performance



%	1m	3m	12m
Abs	0.1	(5.9)	(6.1)
Rel (local)	(3.2)	(5.5)	(4.4)

52-week high/low HK\$10.52 HK\$6.98

Business description

China Water Affairs (CWA) is a pioneer in the privatisation of water supply assets in China. The company seeks to create growth via volume/price increases.

Next events

AGM September 2019

Interim results December 2019

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Although FY19 revenue was below expectations, it was offset by higher than expected margins in the water supply business and a lower tax charge, allowing EPS to beat our forecast. China Water Affairs Group's (CWA's) 2013–19 compound annual growth rate (CAGR) in EPS now stands at over 27% and the group remains positive about its prospects. The current rating is undemanding for a company with CWA's growth prospects.

Year end	Revenue (HK\$m)	PBT* (HK\$m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
03/18	7,580	2,462	71.8	23.0	10.7	3.0
03/19	8,302	2,772	85.1	28.0	9.0	3.6
03/20e	9,703	3,358	96.8	33.0	7.9	4.3
03/21e	11,323	3,907	112.6	38.0	6.8	4.9

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

FY19 results: Another year of growth

CWA's FY19 revenue rose by 9.5%, to HK\$8.3bn, but undershot our expectations (HK\$8.7bn), the result of slower growth in the water supply business due to currency effects and a capex-related decline (-6.6%) in construction services. However, strong growth in water supply revenues (+12.6%, +16.7% before currency effects), connections service revenues (+9.7%, +13.7%) and an improvement in the margin, (from 37% to 41%), resulted in overall water supply profits increasing by 9.0%. The Environmental Protection business continues to grow strongly, posting an 87.1% rise in revenue and a 63.8% increase in segment profits, helped by facilities upgrades and construction work. EPS (basic) of 85.1c was up 17.2% versus 2018 and exceeded our forecast for FY19 of 83.2c, thanks to a lower than anticipated tax rate (23% versus our assumed 28%). Excluding currency fluctuations, y-o-y net profit growth was 25.4%. CWA has achieved a CAGR in EPS for the period 2013–19 of 27.4%. The DPS of 28c (+21.7% y-o-y), undershot our forecast of 30c (2013–19 CAGR of 33%). Net debt increased to HK\$10.3bn with a total liabilities/total assets ratio of 64% (a five-year avg. of 61%).

Outlook: KIEG will contribute for the first time in FY20

CWA remains confident of its prospects and believes recent statements from the Chinese government are supportive of the role of private finance in public infrastructure. The April 2019 acquisition of a 29.5% stake in Kangda International Environmental Group (KIEG) for HK\$1.2bn occurred after the year end. The short-term financial impact of the acquisition (from FY20) is likely to be small but in the long term should help to strengthen CWA's Environmental Protection business.

Valuation: Upside to peer group

We have revised our forecasts and now expect EPS of 96.8c for FY20 (versus 101c previously). Our projections for the period 2019–22 assume a CAGR in EPS of c 16%. At a share price of HK\$8, CWA is trading on an FY20e P/E of 8.3x, a P/B ratio of 1.4x and a PEG ratio of 0.6x compared to peer group averages of 15.6x, 1.6x, and 1.2x, respectively. A PEG ratio of 0.9x would produce an indicative share price of HK\$11 for CWA.

Exhibit 1: Financial summary

	HK\$m	2017	2018	2019	2020e	2021e
Year end 31 March		HKFRS	HKFRS	HKFRS	HKFRS	HKFRS
PROFIT & LOSS						
Water supply revenue		4,874	6,204	6,376	7,225	8,105
Environmental Protection		531	814	1522	2055	2774
Other segments		303	562	404	424	445
Revenue TOTAL		5,708	7,580	8,302	9,703	11,323
EBITDA		2,646	3,097	3,507	4,174	4,860
Operating Profit		2,271	2,691	3,022	3,600	4,211
Amortisation		315	334	404	444	489
Depreciation		60	71	81	130	160
Net Interest expense		(251)	(289)	(319)	(422)	(506)
Profit Before Tax		1,963	2,462	2,772	3,358	3,907
Tax		(583)	(701)	(642)	(940)	(1,094)
Profit After Tax		1,379	1,762	2,130	2,418	2,813
Net profits attributable to shareholders		853	1,141	1,369	1,564	1,820
Average Number of Shares Outstanding (m)		1,505	1,571	1,609	1,609	1,609
EPS - fully diluted (c)		55.4	71.8	85.1	96.8	112.6
Dividend per share (c)		20.0	23.0	28.0	33.0	38.0
EBITDA Margin (%)		46.4	40.9	42.2	43.0	42.9
Operating Margin (%)		39.8	35.5	36.4	37.1	37.2
BALANCE SHEET						
Fixed Assets		15,689	19,581	24,493	28,702	31,636
Intangible Assets		10,316	13,499	16,514	19,569	22,581
Plant, property and equipment		1,127	1,695	2,020	1,990	1,930
Investment properties		1,173	909	912	915	918
Investment in associates		635	661	676	1,676	1,454
Other		2,438	2,817	4,371	4,551	4,753
Current Assets		9,942	9,008	11,332	12,324	10,511
Properties Under Development		690	1,370	1,274	1,274	1,274
Properties Held for Sale		289	597	816	816	816
Inventory		285	348	531	621	724
Trade and Bills Receivables		872	1,055	1,243	1,453	1,695
Due from Non-controlling Equity Holders of Subsidiaries		251	260	288	323	376
Due from Associates		409	563	227	227	227
Prepayments, Deposits and Other Receivables		1,743	1,293	1,550	1,811	2,114
Pledged Deposits		783	570	645	645	645
Deposits and cash		4,314	2,511	3,973	4,370	1,855
Other		307	440	785	784	784
Current Liabilities		7,393	8,649	10,019	12,124	10,065
Trade and Bills Payables		1,097	1,626	2,410	1,400	1,500
Accrued Liabilities, Deposits and Other Payables		2,102	2,306	1,979	2,878	3,365
Short-term Borrowings		3,206	3,450	3,437	5,032	2,040
Other		988	1,267	2,192	2,813	3,160
Long Term Liabilities		9,275	8,786	12,903	14,317	15,534
Long-term Borrowings		8,123	7,432	11,494	12,494	13,494
Other long term liabilities		1,152	1,354	1,409	1,823	2,040
Shareholders' Equity		8,963	11,154	12,902	14,585	16,548
		-	-	-	-	-
CASH FLOW *						
Net Cash Flows from Operating Activities		1,452	1,632	1,429	3,179	3,763
Purchase of property, plant and equipment		(92)	(100)	(100)	(100)	(100)
Increase in concession rights for water supply and sewage processing		(1,808)	(2,500)	(2,500)	(3,500)	(3,500)
Acquisitions/disposals		(283)	0	0	(1,200)	0
Increase in prepayments and other receivables		(1,226)	0	0	0	0
Others		(134)	(171)	(708)	159	164
Net Cash Flows from Investing Activities		(3,543)	(2,771)	(3,308)	(4,641)	(3,436)
Dividends		(135)	(369)	(450)	(531)	(611)
Shares issue and/or options exercised		(38)	301	0	0	0
Other		245	(362)	(183)	(205)	(238)
Net Cash Flow		(2,020)	(1,569)	(2,513)	(2,198)	(523)
Opening net debt (CWA definition)		4,213	6,232	7,801	10,313	12,512
Closing net debt/(cash)		6,232	7,801	10,313	12,512	13,034
Net debt to equity ratio (CWA definition)		70%	70%	80%	86%	79%

Source: Company accounts, Edison Investment Research. Note: *FY19 cash flow figures remain estimates as CWA has yet to publish its cash flow statement for the year.

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