

# Huaneng Renewables (958 HK)

## 1H earnings beat, but lacks re-rating catalyst

HNR, as we expected, was the best performing wind operators among major SOE peers in 1H19. HNR's 1H19 earnings beat our estimates from better-than-expected cost control and significant improvement in finance costs. However, as there is still no clear solution from both the Company and government on subsidy receivables, we think HNR lack of catalyst to sustain further rerating. We cut TP to HK\$2.47, downgrade HNR to HOLD rating.

- 1H19 results beat.** Revenue was RMB7,139mn, up 13.0% YoY. Major expenses were remained in good control, with 1) repairs and maintenance costs down 13.0% YoY and 2) administrative costs down 13.2% YoY. Operating profit increased faster than topline, as a result, to RMB4,651mn. Finance expenses also experienced decline by 7.4% YoY. Mgmt. took active measure through issuing multiple ultra-short-term financing to improve finance costs. Net profit read RMB3,094mn, up 31.7% YoY. HNR's robust 1H19 earnings revealed its strong operating leverage, and the bottom line was 5.0% higher than our estimates.
- Subsidy receivables increased RMB4.1bn during 1H19.** Total subsidy receivables reached RMB12.8bn by 1H19. Mgmt. disclosed subsidy collection was ~RMB0.86bn in 7M19. Based on past subsidy collection history, HNR expects to collect ~RMB3-4bn subsidy in FY19. HNR plans to transfer receivables to Huaneng Group by RMB1bn per year in 2019-21 through ABN product to recycle subsidy receivables. Mgmt. disclosed reference rate would be 5% based on transfer terms, and arrangement fees will be charged in advance with a cap of RMB180mn per year. We believe ABN product can only be served as a short-term measure to slower receivable expansion pace, subsidy receivable will still increase as according to our estimates.
- Slightly adjusting capacity target.** Mgmt. trimmed FY19 capacity addition target slightly from 1.6GW to 1.4GW, and maintained FY20 target unchanged at above 2.0GW. HNR's strategic focus in short-term is to secure FiT projects as much as possible.
- Cut TP to HK\$2.47, downgrade to HOLD.** We raise FY19-21E EPS outlook by 2.5%/4.0%/9.1% based on 1H19 operating updates. However, as subsidy receivable issue was stalled and without a clear solution, we believe HNR's cash flow will be dragged by subsidy receivables despite issuing ABN through parent Co., and market will still be cautious to wind operators. **Our DCF TP is trimmed 11.8% from HK\$2.80 to HK\$2.47. Downgrade to HOLD.**

### Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue (RMB mn)	10,554	11,650	12,625	13,529	15,556
YoY growth (%)	14.2	10.4	8.4	7.2	15.0
Net income (RMB mn)	3,012	3,086	4,116	4,259	4,928
EPS (RMB)	0.29	0.29	0.39	0.40	0.47
YoY growth (%)	7.5	-0.6	33.4	3.5	15.7
P/E (x)	6.6	6.7	5.0	4.8	4.2
P/B (x)	0.8	0.8	0.7	0.6	0.5
Yield (%)	2.2	2.3	3.0	3.1	3.6
ROE (%)	12.2	11.3	13.3	12.3	12.6
Net gearing (%)	189.9	175.7	159.6	158.3	139.2

Source: Company data, CMBIS estimates

**HOLD (Down)**

Target Price	HK\$2.47
(Previous TP)	HK\$2.80)
Up/Downside	+13.8%
Current Price	HK\$2.17

### China Wind Sector

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### Stock Data

Mkt Cap (HK\$ mn)	22,929
Avg 3 mths t/o (HK\$ mn)	36.71
52w High/Low (HK\$)	2.64/1.87
Total Issued Shares (mn)	5,031

Source: Bloomberg

### Shareholding Structure

Huaneng Group	52.4%
Freefloat	47.6%

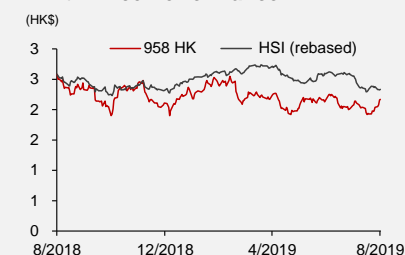
Source: HKEx

### Share Performance

	Absolute	Relative
1-mth	6.9%	18.5%
3-mth	6.9%	14.3%
6-mth	-9.6%	1.0%
12-mth	-17.2%	-8.4%

Source: Bloomberg

### 12-mth Price Performance



Source: Bloomberg

Auditor: KPMG

### Related Reports

- "Huaneng Renewables (958 HK) - Outstanding operating performance in 1H19 - 5 Aug 2019"
- "Huaneng Renewables (958 HK) - 1Q19 earnings surged with increasing operating leverage" 30 Apr 2019
- "Huaneng Renewables (958 HK) - "Mid-term outlook turns gray - 24 Aug 2018"

**Figure 1: 1H19 operating performance vs. FY18 and our estimates**

Company and segment	1H18	1H19	YoY growth (%)	FY18A	FY19E	1H18/ FY18 (%)	1H19/ FY19E (%)
	Power generation (GWh)	Power generation (GWh)		Power generation (GWh)	Power generation (GWh)		
<b>HNR - 958 HK</b>							
<b>Power generation total</b>	<b>13,610</b>	<b>15,196</b>	<b>11.7%</b>	<b>24,974</b>	<b>26,988</b>	<b>54.5%</b>	<b>56.3%</b>
Wind	12,906	14,423	11.7%	23,563	25,472	54.8%	56.6%
Solar	703	773	10.0%	1,410	1,516	49.9%	51.0%

Source: Company data, CMBIS

**Figure 2: HNR's 1H19 results summary**

(RMB mn)	1H18	1H19A	YoY change%	1H19E	1H19A vs. 1H19E	Our comments
<b>Revenue</b>	<b>6,318</b>	<b>7,139</b>	<b>13.0%</b>	<b>7,090</b>	<b>0.7%</b>	<b>In line with our est.</b>
Other net income	191	223	16.6%	158	41.2%	
<b>Operating expenses</b>	<b>-2,643</b>	<b>-2,710</b>	<b>2.5%</b>	<b>-2,636</b>	<b>2.8%</b>	
Depreciation and amortisation	-1,978	-2,036	2.9%	-1,985	2.6%	In line with our estimations
Service concession construction costs	-	-	n/a	-	n/a	
Personnel costs	-225	-276	22.4%	-247	11.4%	
Repairs and maintenance	-111	-97	-13.0%	-101	-4.1%	Resume normal from shuffel in 2018
Administration expenses	-120	-104	-13.2%	-130	-20.1%	Gained better control during 1H19
Other operating expenses	-209	-198	-5.4%	-172	14.8%	
<b>Operating profit</b>	<b>3,867</b>	<b>4,651</b>	<b>20.3%</b>	<b>4,613</b>	<b>0.8%</b>	<b>In line with our est.</b>
<b>Net finance expenses</b>	<b>-1,058</b>	<b>-972</b>	<b>-8.2%</b>	<b>-1,081</b>	<b>-10.1%</b>	
Finance income	45	50	11.5%	54	-7.4%	Took active UST financing to reduce interest rate
Finance expenses	-1,103	-1,022	-7.4%	-1,135	-10.0%	
Other gains or loss	1	9	750.9%	-	n/a	
Share of loss of a JV and associate	-9	8	-189.0%	-2	-474.0%	
<b>Profit before taxation</b>	<b>2,800</b>	<b>3,696</b>	<b>32.0%</b>	<b>3,529</b>	<b>4.7%</b>	
Income tax	-399	-546	36.7%	-528	3.3%	
Effective tax rate	14.3%	14.8%	3.5%	15.0%	-0.2ppt	In line.
<b>Profit of the year</b>	<b>2,400</b>	<b>3,150</b>	<b>31.3%</b>	<b>3,001</b>	<b>5.0%</b>	<b>Beat our est.</b>
Less: non-controlling interests	-51	-57	11.0%	-54	5.0%	
<b>Net profit</b>	<b>2,349</b>	<b>3,094</b>	<b>31.7%</b>	<b>2,947</b>	<b>5.0%</b>	<b>Beat our est.</b>
Net profit margin	37.2%	43.3%	16.6%	41.6%	1.8ppt	

Source: Company data, CMBIS estimates

**Figure 3: Earnings revision**

	Old			New			Change(%)		
	2019	2020	2021	2019	2020	2021	2019	2020	2021
Revenue (Rmb mn)	12,593	13,519	15,045	12,625	13,529	15,556	0.3%	0.1%	3.4%
Net Income (Rmb mn)	4,015	4,096	4,515	4,116	4,259	4,928	2.5%	4.0%	9.1%
EPS (Rmb)	0.38	0.39	0.43	0.39	0.40	0.47	2.5%	4.0%	9.1%

Source: CMBIS estimates

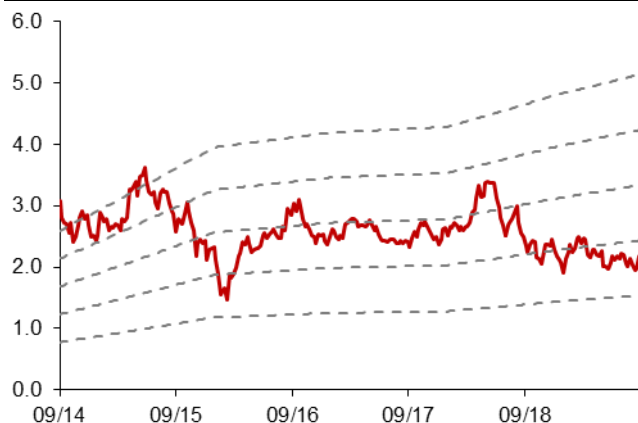
Figure 4: Our DCF valuation

DCF Valuation	2020E	2021E	2022E	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E
<b>Grid Connected Capacity(MW)</b>	<b>15,465</b>	<b>16,715</b>	<b>17,965</b>	<b>19,215</b>	<b>20,560</b>	<b>22,000</b>	<b>23,540</b>	<b>25,187</b>	<b>26,951</b>	<b>28,837</b>	<b>30,856</b>
Capacity growth	15%	8%	7%	7%	7%	7%	7%	7%	7%	7%	7%
Additional capacity of that year(MW)	2,050	1,250	1,250	1,250	1,345	1,439	1,540	1,648	1,763	1,887	2,019
<b>Turnover</b>	<b>13,529</b>	<b>15,556</b>	<b>16,613</b>	<b>17,642</b>	<b>16,942</b>	<b>18,084</b>	<b>19,303</b>	<b>20,603</b>	<b>21,992</b>	<b>23,473</b>	<b>25,055</b>
Turnover growth	7%	15%	7%	6%	-4%	7%	7%	7%	7%	7%	7%
<b>EBIT (Rmb mn)</b>	<b>7,382</b>	<b>8,440</b>	<b>8,895</b>	<b>9,306</b>	<b>8,791</b>	<b>9,228</b>	<b>9,684</b>	<b>10,160</b>	<b>10,655</b>	<b>11,171</b>	<b>11,709</b>
EBIT margin	55%	54%	54%	53%	52%	51%	50%	49%	48%	48%	47%
Tax rate	16%	16%	16%	17%	14%	15%	16%	16%	16%	17%	17%
Depreciation -Rmb mn	4,519	5,191	5,604	6,016	5,574	5,950	6,351	6,778	7,235	7,723	8,243
CAPEX (Rmb mn)	(14,875)	(9,010)	(8,985)	(8,960)	(9,566)	(10,185)	(10,843)	(11,544)	(12,291)	(13,085)	(14,001)
Invest in working capital	1,265	252	(527)	(763)	210	(343)	(366)	(390)	(416)	(445)	(474)
<b>Free cash flow</b>	<b>(2,912)</b>	<b>3,490</b>	<b>3,524</b>	<b>4,030</b>	<b>3,754</b>	<b>3,284</b>	<b>3,314</b>	<b>3,378</b>	<b>3,440</b>	<b>3,501</b>	<b>3,490</b>
<b>Years</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>8</b>	<b>9</b>	<b>10</b>	<b>11</b>
Discount factor	0.94	0.88	0.83	0.78	0.73	0.69	0.64	0.61	0.57	0.53	0.50
Discount free cash flow	(2,735)	3,079	2,920	3,137	2,744	2,255	2,137	2,046	1,957	1,871	1,751
<b>Terminal value</b>	<b>103,669</b>										
<b>Terminal perpetual growth</b>	<b>3%</b>										
<b>Terminal EV/EBITDA</b>	<b>5.20</b>										

Valuations (Rmb mn)		WACC Calculations	
<b>Terminal value</b>	<b>103,669</b>	Cost of debt	4.9%
Terminal perpetual growth	3.0%	Tax rate	16.5%
Terminal EV/EBITDA	5.20	After tax cost of debt	4.1%
Total discount FCF	21,162	Cost of equity	13.6%
Discount terminal value	52,033	Adjusted beta	0.80
Firm value	73,195	Market risk premium	14.7%
Discount FCF(% of total)	28.9%	Risk free rate	1.8%
Terminal value (% of total)	71.1%	% of debt financing	75.0%
Add: Cash & cash equivalent	3,551	<b>WACC</b>	<b>6.5%</b>
Less: Debt	52,391		
Non-controlling interest	835		
Equity Value - Rmb	23,520		
<b>Share fair value (Rmb)</b>	<b>2.23</b>		
<b>Exchange rate (HKD/Rmb)</b>	<b>0.90</b>		
<b>Share fair value (HKD)</b>	<b>2.47</b>		

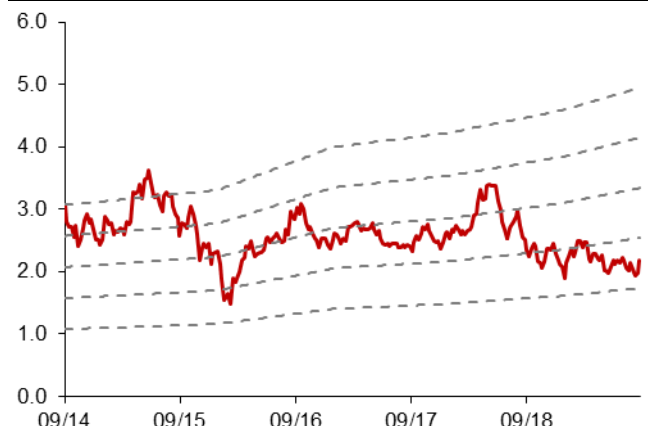
Source: CMBIS estimates

Figure 5: 12M forward P/E band



Source: Company data, CMBIS

Figure 6: 12M forward P/B band



Source: Company data, CMBIS

## Financial Summary

### Income statement

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
<b>Revenue</b>	<b>10,554</b>	<b>11,650</b>	<b>12,625</b>	<b>13,529</b>	<b>15,556</b>
Wind	9,617	10,611	11,530	12,408	14,401
Solar	937	1,039	1,094	1,121	1,155
<b>Other net income</b>	<b>469</b>	<b>388</b>	<b>385</b>	<b>427</b>	<b>489</b>
<b>Operating expenses</b>	<b>(5,372)</b>	<b>(6,142)</b>	<b>(5,929)</b>	<b>(6,574)</b>	<b>(7,606)</b>
DD&A	(3,798)	(3,973)	(4,076)	(4,519)	(5,191)
Personnel costs	(514)	(652)	(704)	(811)	(978)
Repair and maintenance	(191)	(265)	(253)	(284)	(333)
Administrative exps	(248)	(273)	(290)	(311)	(358)
Other operating exps	(621)	(980)	(606)	(649)	(747)
<b>EBIT</b>	<b>5,651</b>	<b>5,896</b>	<b>7,080</b>	<b>7,382</b>	<b>8,440</b>
Finance costs, net	(2,238)	(2,189)	(2,071)	(2,245)	(2,454)
JV & Associates	(5)	(11)	(8)	(8)	(8)
Exceptional	-	-	-	-	-
<b>Pre-tax profit</b>	<b>3,408</b>	<b>3,695</b>	<b>5,001</b>	<b>5,128</b>	<b>5,977</b>
Income tax	(346)	(567)	(826)	(809)	(979)
Less: Minority interests	50	42	58	60	70
<b>Net profit</b>	<b>3,012</b>	<b>3,086</b>	<b>4,116</b>	<b>4,259</b>	<b>4,928</b>

### Cash flow summary

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
<b>Net income</b>	<b>3,012</b>	<b>3,086</b>	<b>4,116</b>	<b>4,259</b>	<b>4,928</b>
DD&A	3,804	3,977	4,081	4,524	5,247
Change in working capital	(3,792)	(1,780)	600	1,265	252
Others	(804)	(1,184)	966	(302)	(121)
<b>CF from operation</b>	<b>2,220</b>	<b>4,099</b>	<b>9,763</b>	<b>9,747</b>	<b>10,306</b>
Capex & investments	(3,219)	(3,298)	(11,353)	(14,866)	(9,001)
Associated companies	1,061	250	468	339	(21)
Others	336	-	-	-	-
<b>CF from investments</b>	<b>(2,158)</b>	<b>(3,048)</b>	<b>(10,885)</b>	<b>(14,526)</b>	<b>(9,022)</b>
Equity raised	1,852	-	-	-	-
Change of Debts	(1,566)	40	1,694	7,057	2,578
Dividend paid	(399)	(454)	(465)	(617)	(639)
Others	(17)	275	30	30	30
<b>CF from financing</b>	<b>(129)</b>	<b>(140)</b>	<b>1,259</b>	<b>6,469</b>	<b>1,969</b>
<b>Net change in cash</b>	<b>(67)</b>	<b>912</b>	<b>136</b>	<b>1,690</b>	<b>3,252</b>
Cash at year begin	2,570	2,503	3,415	3,551	5,241
Exchange difference	-	-	-	-	-
<b>Cash at the end of the year</b>	<b>2,503</b>	<b>3,415</b>	<b>3,551</b>	<b>5,241</b>	<b>8,493</b>
Less: pledged cash	52	68	63	66	66

### Balance sheet

YE Dec 31 (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
<b>Non-current assets</b>	<b>75,107</b>	<b>74,089</b>	<b>80,904</b>	<b>90,917</b>	<b>94,703</b>
Fixed asset	71,406	70,812	78,119	88,497	92,288
Prepaid lease payments	357	269	280	291	301
Interest in JVs	254	201	199	196	194
Other non-current assets	3,090	2,807	2,306	1,933	1,920
<b>Current assets</b>	<b>11,242</b>	<b>14,582</b>	<b>15,531</b>	<b>17,940</b>	<b>21,451</b>
Cash	2,503	3,415	3,551	5,241	8,493
Account receivable	7,214	9,968	10,574	11,284	11,539
Prepayments	1,396	1,069	1,276	1,276	1,276
Other current assets	130	130	130	139	142
<b>Current liabilities</b>	<b>27,086</b>	<b>29,031</b>	<b>32,237</b>	<b>37,543</b>	<b>39,188</b>
Borrowings	20,353	21,614	23,576	26,886	28,181
Finance leases	352	472	300	300	130
Other payables	6,253	6,817	8,241	10,236	10,756
Tax payables	128	128	120	120	120
<b>Non-current liabilities</b>	<b>33,821</b>	<b>31,427</b>	<b>32,304</b>	<b>35,749</b>	<b>37,080</b>
Borrowings	29,451	28,611	28,815	32,861	34,444
Finance leases	1,231	730	430	130	-
Deferred income	198	181	189	185	187
Others	2,940	1,905	2,870	2,572	2,449
<b>Total equity</b>	<b>25,442</b>	<b>28,214</b>	<b>31,895</b>	<b>35,566</b>	<b>39,886</b>
<b>Minority Interest</b>	<b>840</b>	<b>805</b>	<b>835</b>	<b>865</b>	<b>895</b>
<b>Shareholders' equity</b>	<b>24,602</b>	<b>27,408</b>	<b>31,059</b>	<b>34,701</b>	<b>38,991</b>

### Key ratios

YE Dec 31	FY17A	FY18A	FY19E	FY20E	FY21E
<b>Sales mix (%)</b>					
Wind	91.1	91.1	91.3	91.7	92.6
Solar	8.9	8.9	8.7	8.3	7.4
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
<b>P&amp;L ratios (%)</b>					
Operating margin	53.5	50.6	56.1	54.6	54.3
Pre-tax margin	32.3	31.7	39.6	37.9	38.4
Net margin	28.5	26.5	32.6	31.5	31.7
Effective tax rate	-10.2	-15.3	-16.5	-15.8	-16.4
<b>Balance sheet ratios</b>					
Current ratio (x)	0.42	0.50	0.48	0.48	0.55
Quick ratio (x)	0.41	0.50	0.48	0.48	0.55
Cash ratio (x)	0.17	0.12	0.11	0.14	0.22
Debtors turnover days	205	269	297	295	268
Total debt / total equity (%)	180	178	164	168	157
Net debt / equity (%)	190	176	160	158	139
<b>Returns (%)</b>					
ROE	12.2	11.3	13.3	12.3	12.6
ROA	3.5	3.5	4.3	3.9	4.2
<b>Per share</b>					
EPS (RMB)	0.29	0.29	0.39	0.40	0.47
DPS (RMB)	0.04	0.04	0.06	0.06	0.07
BVPS (RMB)	2.33	2.59	2.94	3.28	3.69

Source: Company data, CMBIS estimates

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**BUY** : Stock with potential return of over 15% over next 12 months  
**HOLD** : Stock with potential return of +15% to -10% over next 12 months  
**SELL** : Stock with potential loss of over 10% over next 12 months  
**NOT RATED** : Stock is not rated by CMBIS

**OUTPERFORM** : Industry expected to outperform the relevant broad market benchmark over next 12 months  
**MARKET-PERFORM** : Industry expected to perform in-line with the relevant broad market benchmark over next 12 months  
**UNDERPERFORM** : Industry expected to underperform the relevant broad market benchmark over next 12 months

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