

NWS Holdings (659 HK)

Impact of Toll Fee Exemption

The Ministry of Transport of the PRC announced that effective from 17 Feb, until the end of the prevention and control measures taken by the government over COVID-19, all vehicles that travel on toll roads will be exempted from toll fee, in order to facilitate the resumption of business and production and to sustain economic growth.

- Roads/overall AOP to drop by 54%/17% in FY20E in base case.** Having considered the impact of COVID-19 and toll fee exemption, in our best/base/worst case scenarios, we estimate that NWS's Roads segment's attributable operating profit (AOP) would drop by 31%/54%/86% in FY20E, and overall AOP would drop by 10%/17%/28%.
- Expect protective policies to mitigate the impact.** MoT's announcement stated that it would consider launching "relevant ancillary protective measures to protect the rights of toll roads users, creditors, investors and operators". We believe possible protective measures include government subsidy or tax rebate to toll roads operators, extending toll roads' concession rights, and interest rate cut on their bank loans or extension of loan repayment. We have not factored in any protective measures into our model.
- Balance sheet remains strong.** Despite the fact that toll fee exemption would hurt cash flow of NWS, its balance sheet would remain strong even after splashing out HK\$21.5bn to acquire FTLife in 2019, with ample cash on hand and healthy net gearing (we estimate cash to be HK\$8.4bn and net gearing 33% as at 30 Jun 2020) and unutilised committed banking facilities (HK\$12.4bn as at 30 Jun 2019).
- Committed to progressive dividend policy.** In the annual results announcement in Sep 2019, NWS announced a new progressive dividend policy, i.e. to steadily increase or at least maintain the HKD value of ordinary DPS annually. NWS reiterated in its announcement on 17 Feb to maintain its existing sustainable and progressive dividend policy.
- Maintain BUY as a yield play.** We revise down TP from HK\$15.40 to HK\$14.06, based on 20% discount to FY20E NAV. COVID-19 will adversely impact NWS only in the short term. Long-term fundamentals are intact. NWS remains an attractive yield play, with 5.7% FY20E dividend yield.

Earnings Summary

| (YE 30 Jun) | FY18A | FY19A | FY20E | FY21E | FY22E |
|---|--------|--------|--------|--------|--------|
| Revenue (HK\$ mn) | 35,115 | 26,834 | 34,369 | 38,716 | 39,781 |
| Attributable operating profit (HK\$ mn) | 5,232 | 4,707 | 4,838 | 6,991 | 7,655 |
| YoY growth (%) | 8.1 | (10.0) | 2.8 | 44.5 | 9.5 |
| Profit to shareholders (HK\$ mn) | 6,069 | 4,043 | 3,439 | 5,440 | 6,160 |
| EPS (HK\$) | 1.56 | 1.04 | 0.88 | 1.39 | 1.57 |
| YoY growth (%) | 6.6 | (33.4) | (15.1) | 58.2 | 13.2 |
| P/E (x) | 7.4 | 10.1 | 11.9 | 7.5 | 6.6 |
| P/B (x) | 0.90 | 0.83 | 0.81 | 0.76 | 0.71 |
| Yield (%) | 6.7 | 5.5 | 5.7 | 6.0 | 6.3 |
| ROE (%) | 12.3 | 8.2 | 6.9 | 10.4 | 11.1 |
| Net gearing (%) | 7.0 | 0.0 | 32.5 | 28.5 | 22.8 |

Source: Company data, CMBIS estimates

BUY (Maintain)

| | |
|---------------|-----------|
| Target Price | HK\$14.06 |
| (Previous TP) | HK\$15.40 |
| Up/Downside | +34.4% |
| Current Price | HK\$10.46 |

Conglomerate Sector

Daniel So, CFA
 (852) 3900 0857
 danielso@cmbi.com.hk

Stock Data

| | |
|--------------------------|-------------|
| Mkt Cap (HK\$ mn) | 40,911 |
| Avg 3 mths t/o (HK\$ mn) | 31.68 |
| 52w High/Low (HK\$) | 21.9 / 9.85 |
| Total Issued Shares (mn) | 3,911.1 |

Source: Bloomberg

Shareholding Structure

| | |
|-------------------------|--------|
| New World Development | 60.86% |
| Chow Tai Fook (Holding) | 2.49% |

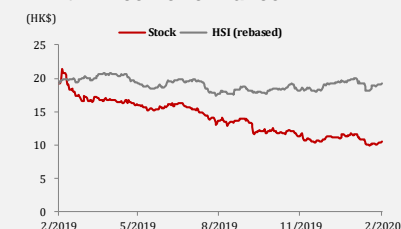
Source: HKEx

Share Performance

| | Absolute | Relative |
|-------|----------|----------|
| 1-mth | -10.1% | -6.6% |
| 3-mth | -7.1% | -12.5% |
| 6-mth | -23.6% | -29.7% |

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: PricewaterhouseCoopers

Related Reports:

- NWS Holdings (659 HK) – Road to recovery – takeaways from tour – 21 Jan 2020
- NWS Holdings (659 HK) – FTLife acquisition to drive earnings recovery – 5 Nov 2019
- NWS Holdings (659 HK) – Results missed but worst is over – 26 Sep 2019
- NWS Holdings (659 HK) – Initiation: Adding growth to defensive business – 19 Jul 2019

Toll Fee Exemption during COVID-19 outbreak

On 15 Feb 2020, the Ministry of Transport (MoT) of the PRC issued the **Notice on the implementation of the Toll Fee Exemption*** which took effect from 0:00 a.m. on 17 Feb 2020, until the end of the prevention and control measures taken by the PRC Government over COVID-19. The Toll Fee Exemption applies to all vehicles that travel on toll roads (including toll bridges and tunnels) in the PRC that have been constructed pursuant to approval granted under the Highway Law of the People's Republic of China and the Regulations on the Administration of Toll Roads of the PRC.

The aim of this new policy is to facilitate the resumption of business and production and to sustain economic growth.

**MoT's notice*: 交通运输部关于新冠肺炎疫情防控期间免收收费公路车辆通行费的通知
http://www.mot.gov.cn/jiaotongyaowen/202002/t20200215_3333512.html

Expect protective policies to mitigate the impact

MoT's also stated that it would consider launching "relevant ancillary protective measures to protect the rights of toll roads users, creditors, investors and operators" ("将另行研究出台相关配套保障政策，统筹维护收费公路使用者、债权人、投资者和经营者的合法权益"). While there are no details at this stage, we believe possible protective measures include government subsidy or tax rebate to toll roads operators, extending toll roads' concession rights, and interest rate cut on their bank loans or extension of loan repayment.

Financial impact on NWS

Roads contributed >30% of profit

NWS has four "Core Business" segments, namely Roads, Aviation, Construction and Insurance (acquired FTLife in Nov 2019). In FY19 (ended 30 Jun 2019), the Roads segment contributed to 39% of the attributable operating profit (AOP) of NWS. In our base case assumption (see "Scenario analysis" below), we estimate the Roads segment would contribute to 18% of AOP in FY20E following a decrease in toll fee income. Besides, this year's AOP will include contribution from FTLife.

Scenario analysis

Toll fee exemption will significantly hurt the cash flow and earnings of the Roads segment as long as the exemption is effective, as the majority of toll roads' costs are fixed. The magnitude of financial impact depends on the duration of the exemption period.

Even before the implementation of toll fee exemption, toll roads traffic were already badly hit by COVID-19. The MoT said on 15 Feb that 1) this year's 40-day Spring Festival travel rush ("春运") has recorded a 45% YoY drop in number of passengers; 2) between 25 Jan-14 Feb, number of passengers slumped 82% YoY; 3) since 9 Feb, number of vehicles passing through highways decreased 78% YoY.

Our assumptions in scenario analysis are as follows:

- 1) Base case: Epidemic ends in late-Mar 2020, so does the toll fee exemption
- 2) Best case: Epidemic ends in late-Feb 2020, so does the toll fee exemption
- 3) Worst case: Epidemic lingers for longer, and the toll fee exemption ends in mid-May 2020

Having considered the impact of COVID-19 and toll fee exemption, in our best/base/worst case scenarios, we estimate that NWS's Roads segment's attributable operating profit (AOP) would drop by 31%/54%/86% in FY20E, and overall AOP would drop by 10%/17%/28%.

We have not factored in any protective policies into our model.

Figure 1: Scenario analysis

| | Best case | Base case | Worst case |
|--------------------------------------|---------------|----------------------|--------------|
| Assumption: Toll fee exemption until | Late-Feb 2020 | Late-Mar 2020 | Mid-May 2020 |
| Roads revenue impact | -11% | -19% | -32% |
| Roads AOP impact | -31% | -54% | -86% |
| Group AOP impact | -10% | -17% | -28% |
| Group EPS impact | -12% | -20% | -33% |

Source: CMBIS estimates

Balance sheet remains strong

Despite the fact that toll fee exemption would hurt cashflow of NWS, its balance sheet would remain strong even after splashing out HK\$21.5bn to acquire FTLife in 2019, with ample cash on hand and healthy net gearing (we estimate cash to be HK\$8.4bn and net gearing 33% as at 30 Jun 2020) and unutilised committed banking facilities (HK\$12.4bn as at 30 Jun 2019).

Committed to progressive dividend policy

In the annual results announcement in Sep 2019, NWS announced a new progressive dividend policy, i.e. to steadily increase or at least maintain the HKD value of ordinary DPS annually. NWS reiterated in its announcement on 17 Feb to maintain its existing sustainable and progressive dividend policy.

Reiterate BUY, TP cut to HK\$14.06

While COVID-19 and the toll fee exemption policy will significantly drag NWS's AOP and EPS in the short term (probably for two to five months), and thereby delay its earnings recovery to FY21, its long-term fundamentals are intact. **We revised down FY20E NAV to HK\$17.58 using sum-of-the-parts, and target price from HK\$15.40 to HK\$14.06, based on 20% discount to NAV.**

NWS remains an attractive yield play, with 5.7% FY20E dividend yield and earnings growth potential from its Core Business segments. Potential catalysts include disposals of non-core assets, spin-offs (e.g. aircraft leasing) and acquisitions of assets under Core Business.

Figure 2: NAV by sum-of-the-parts

| | Valuation method | FY20E GAV (HK\$m) | FY20E GAV per share (HK\$) | % of GAV |
|-------------------------------------|---------------------------|----------------------|-------------------------------|-------------|
| Roads | | 20,140 | 5.15 | 20% |
| Subsidiaries | DCF: WACC 7.1% | 15,381 | 3.93 | 16% |
| Associates & JVs | P/E: 10.2x | 4,758 | 1.22 | 5% |
| Aviation (Goshawk) | P/E: 9x | 6,415 | 1.64 | 7% |
| Construction | | 9,094 | 2.33 | 9% |
| Construction | P/E: 8.5x | 8,156 | 2.09 | 8% |
| Wai Kee | Market value: HK\$4.74/sh | 939 | 0.24 | 1% |
| Insurance | P/EV: 1.34x | 22,083 | 5.65 | 22% |
| Environment | | 7,363 | 1.88 | 7% |
| SUEZ NWS | P/E: 12.7x | 3,683 | 0.94 | 4% |
| Derun Environment | Committed capital | 2,072 | 0.53 | 2% |
| Power | P/E: 9.7x | 1,608 | 0.41 | 2% |
| Logistics | | 19,277 | 4.93 | 20% |
| ATL Logistics Centre | Cap rate: 4.5% | 17,039 | 4.36 | 17% |
| CUIRC | P/E: 12x | 1,260 | 0.32 | 1% |
| Xiamen port | P/E: 10.2x | 978 | 0.25 | 1% |
| Facilities Management | | 8,661 | 2.21 | 9% |
| HKCEC & Free Duty | DCF: WACC 6.2% | 6,661 | 1.70 | 7% |
| Gleneagles HK | Committed capital | 2,000 | 0.51 | 2% |
| Transport | P/E: 8x | -22 | -0.01 | 0% |
| Strategic investments | Book value | 9,360 | 2.39 | 9% |
| Less Head office expense | P/E: 5x | (3,750) | (0.96) | -4% |
| Gross Asset Value (GAV) | | 98,620 | 25.22 | |
| Less Net debt de facto | | (29,877) | (7.64) | |
| Net Asset Value (NAV) | | 68,743 | 17.58 | |
| Current discount to FY20E NAV | 40% | Current share price | HK\$10.46 | |
| Target discount to FY20E NAV | 20% | Target price | HK\$14.06 | |

Source: Company data, CMBIS estimates

Financial Summary

| Income statement | | | | | | Cash flow summary | | | | | |
|-----------------------------------|---------------|---------------|---------------|---------------|---------------|---------------------------------|----------------|----------------|-----------------|----------------|----------------|
| YE 30 Jun (HK\$ mn) | FY18A | FY19A | FY20E | FY21E | FY22E | YE 30 Jun (HK\$ mn) | FY18A | FY19A | FY20E | FY21E | FY22E |
| Revenue | 35,115 | 26,834 | 34,369 | 38,716 | 39,781 | Operating profit | 5,126 | 2,655 | 2,937 | 4,077 | 4,319 |
| Roads | 2,624 | 2,529 | 2,056 | 2,641 | 2,728 | Adjustments | | | | | |
| Aviation | 161 | 162 | - | - | - | Depreciation & amortization | 1,487 | 1,482 | 1,443 | 1,481 | 1,520 |
| Facilities Management | 5,571 | 4,152 | 4,152 | 4,318 | 4,447 | Other non-cash items | (2,530) | (923) | (500) | (500) | (500) |
| Construction | 26,760 | 16,211 | 19,190 | 20,116 | 20,709 | Working capital changes | | | | | |
| Insurance | - | - | 5,069 | 7,641 | 7,794 | Inventories | 22 | 33 | - | - | - |
| Cost of sales | (31,332) | (23,791) | (30,002) | (32,938) | (33,747) | Trade & other receivables | (787) | 360 | (5,550) | (2,267) | (556) |
| Gross profit | 3,783 | 3,043 | 4,367 | 5,778 | 6,035 | Trade & other payables | 859 | (551) | 3,493 | 1,338 | 369 |
| Other income/gains | 2,809 | 1,030 | 500 | 500 | 500 | Other items | 983 | (13) | (13) | (13) | (13) |
| General and administrative | (1,466) | (1,418) | (1,931) | (2,201) | (2,215) | Net cash from operations | 5,159 | 3,043 | 1,810 | 4,116 | 5,139 |
| Operating profit | 5,126 | 2,655 | 2,937 | 4,077 | 4,319 | Dividends from associates | 542 | 485 | 626 | 1,024 | 1,264 |
| Finance costs | (348) | (452) | (911) | (858) | (763) | Dividends from JV | 1,845 | 1,888 | 1,888 | 2,515 | 2,707 |
| Associated companies | 756 | 759 | 626 | 1,024 | 1,264 | Capital expenditures | (536) | (648) | (577) | (577) | (577) |
| JV | 1,331 | 1,949 | 1,888 | 2,515 | 2,707 | Other investing activities | (344) | (5,240) | (22,217) | (1,639) | (1,639) |
| Profit before income tax | 6,866 | 4,911 | 4,539 | 6,758 | 7,528 | Net cash from investing | 1,507 | (3,516) | (20,279) | 1,323 | 1,756 |
| Income tax expenses | (745) | (652) | (491) | (695) | (741) | Change in borrowings | 444 | (159) | 13,083 | (2,000) | (2,000) |
| Profit for the year | 6,121 | 4,259 | 4,048 | 6,062 | 6,787 | Dividends paid | (5,570) | (2,927) | (2,308) | (2,405) | (2,526) |
| Perpetual capital securities | - | (187) | (582) | (582) | (582) | Other financing activities | 12 | 12,957 | 1,915 | (425) | (425) |
| Non-controlling interests | (52) | (29) | (27) | (41) | (46) | Net cash from financing | (5,115) | 9,871 | 12,690 | (4,830) | (4,951) |
| Net profit to shareholders | 6,069 | 4,043 | 3,439 | 5,440 | 6,160 | Net change in cash | 821 | 8,473 | (6,653) | (469) | 821 |
| | | | | | | Cash at the beginning of year | 6,437 | 6,643 | 15,045 | 8,392 | 7,923 |
| | | | | | | Currency translation diff. | 39 | (70) | - | - | - |
| | | | | | | Cash at the end of year | 7,297 | 15,045 | 8,392 | 7,923 | 8,744 |

| Balance sheet | | | | | | Key ratios | | | | | |
|----------------------------------|---------------|---------------|----------------|----------------|----------------|-----------------------------|-------|-------|-------|-------|-------|
| YE 30 Jun (HK\$ mn) | FY18A | FY19A | FY20E | FY21E | FY22E | YE 30 Jun | FY18A | FY19A | FY20E | FY21E | FY22E |
| Non-current assets | 55,507 | 56,580 | 119,113 | 120,331 | 121,685 | AOP mix (%) | | | | | |
| Property, plant & equip. | 5,370 | 5,413 | 5,418 | 5,384 | 5,311 | Roads | 37.2 | 38.4 | 17.9 | 29.8 | 29.0 |
| Intangible concession right | 11,492 | 10,061 | 14,689 | 14,122 | 13,556 | Aviation | 13.3 | 10.6 | 14.7 | 11.2 | 11.3 |
| Associated companies | 13,763 | 14,552 | 16,008 | 17,608 | 19,369 | Construction | 20.2 | 25.6 | 28.3 | 21.7 | 21.5 |
| Joint ventures | 15,008 | 13,645 | 13,509 | 13,374 | 13,240 | Insurance | - | - | 16.1 | 17.2 | 17.6 |
| Other non-current assets | 9,874 | 12,908 | 69,491 | 69,843 | 70,209 | Environment | 9.4 | 13.4 | 10.0 | 7.6 | 7.2 |
| | | | | | | Logistics | 12.5 | 13.8 | 13.1 | 9.3 | 8.7 |
| Current assets | 19,267 | 29,485 | 29,107 | 30,905 | 32,282 | Facilities Management | (1.4) | (8.4) | (6.8) | (1.7) | (0.2) |
| Cash and bank balances | 6,657 | 15,059 | 8,392 | 7,923 | 8,744 | Transport | 3.0 | (0.2) | (0.1) | 0.3 | 0.6 |
| Trade & other receivables | 12,149 | 13,998 | 19,547 | 21,815 | 22,371 | Strategic Investments | 5.8 | 6.8 | 6.6 | 4.6 | 4.2 |
| Other current assets | 462 | 429 | 1,168 | 1,168 | 1,168 | | | | | | |
| Assets held-for-sale adj. | 151 | - | - | - | - | P&L ratios (%) | | | | | |
| | | | | | | Operating margin | 14.6 | 9.9 | 8.5 | 10.5 | 10.9 |
| Current liabilities | 12,995 | 13,729 | 20,584 | 21,922 | 22,291 | Net margin | 17.3 | 15.1 | 10.0 | 14.1 | 15.5 |
| Borrowings | 1,035 | 2,403 | 4,403 | 4,403 | 4,403 | | | | | | |
| Trade & other payables | 11,384 | 10,843 | 14,336 | 15,674 | 16,043 | Balance sheet ratios | | | | | |
| Other current liabilities | 576 | 483 | 1,845 | 1,845 | 1,845 | Current ratio (x) | 1.48 | 2.15 | 1.41 | 1.41 | 1.45 |
| | | | | | | Quick ratio (x) | 1.45 | 2.12 | 1.39 | 1.39 | 1.43 |
| Non-current liabilities | 11,807 | 15,089 | 66,833 | 65,378 | 64,003 | Net debt / equity ratio (%) | 7.0 | 0.0 | 32.5 | 28.5 | 22.8 |
| Borrowings | 9,140 | 12,666 | 23,749 | 21,749 | 19,749 | | | | | | |
| Debt securities | - | 2,262 | 2,262 | 2,262 | 2,262 | Returns (%) | | | | | |
| Other non-current liabilities | 2,490 | 161 | 40,822 | 41,367 | 41,992 | ROE | 12.3 | 8.2 | 6.9 | 10.4 | 11.1 |
| | | | | | | ROA | 7.9 | 4.9 | 2.9 | 3.6 | 4.0 |
| Shareholders' funds | 49,950 | 49,046 | 50,515 | 53,640 | 57,366 | Per share (HK\$) | | | | | |
| Perpetual capital securities | - | 8,040 | 10,117 | 10,117 | 10,117 | EPS | 1.56 | 1.04 | 0.88 | 1.39 | 1.57 |
| Non-controlling interests | 174 | 161 | 171 | 180 | 190 | DPS | 0.78 | 0.58 | 0.60 | 0.63 | 0.66 |
| Total equity | 50,124 | 57,247 | 60,803 | 63,936 | 67,673 | BVPS | 12.8 | 12.6 | 12.9 | 13.7 | 14.7 |

Source: Company data, CMBIS estimates

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CMB International Securities Limited

Address: 45/F, Champion Tower, 3 Garden Road, Hong Kong, Tel: (852) 3900 0888 Fax: (852) 3900 0800

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