

# NWS Holdings (659 HK)

## Recovery delayed by virus outbreak

NWS's interim earnings for the six months ended 31 Dec 2019 declined (AOP / EPS -6% / -34% YoY) and missed our estimates by 16% / 7%, mainly dragged by non-core segments. Interim DPS maintained at HK\$0.29. Earnings recovery will be delayed by COVID-19 which significantly hit Roads segment. Expect strong recovery in FY21 on low base and full-year contribution from FTLife.

- **Core Business maintained growth.** All of the Core Business segments posted growth in 1H20, and the newly acquired FTLife contributed to 7% of Group's Attributable Operating Profit (AOP) in just two months. Core Business accounted for 89% of AOP in 1H20, up from 75% in FY19.
- **Non-core business deteriorated.** The significant drop in earnings was mainly from Strategic Portfolio (non-core), among which Facilities Mgmt's negative AOP widened by 148% to HK\$364mn, or -16% of Group's AOP. Free Duty suffered badly from challenging tourism and retail environment in HK.
- **COVID-19 to hurt 2H20E earnings.** The COVID-19 outbreak in Jan 2020 will put Facilities Mgmt under further pressure, and cause significant drop in AOP of the core Roads segment. Therefore, the Group's earnings recovery will be delayed to FY21E instead of FY20E as forecasted before the virus outbreak.
- **Long-term prospects intact.** Expect Roads to return to normal once the outbreak is under control (and Facilities Mgmt to recover more gradually). On the plus side, virus outbreak might present M&A opportunities at distressed valuation, e.g. in toll roads. The management mentioned renewable energy and data centre as other possible targets.
- **Potential catalysts:** 1) China's protective policies to compensate for Roads' toll exemption; 2) spinoff (e.g. aviation); 3) disposals of non-core assets such as Transport; 4) acquisitions at attractive valuation; 5) share buyback.
- **Maintain BUY, TP cut to HK\$13.00.** We revise FY20E AOP / EPS by -13% / -15%, and NAV by -1.1%. TP is cut from HK\$14.06 to HK\$13.00, based on 25% discount to FY20E NAV (vs. 20% before). A larger discount reflects lower economic forecasts of China & HK economic growth and wider discounts in other conglomerates' valuation. Trading at 0.76x P/B, a historical low, it remains an attractive yield play with 6.3% FY20E dividend yield.

### Earnings Summary

(YE 30 Jun)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (HK\$ mn)	35,115	26,834	33,675	38,359	39,850
Attributable operating profit (HK\$ mn)	5,232	4,707	4,067	6,375	7,086
YoY growth (%)	8.1	(10.0)	(13.6)	56.8	11.2
Profit to shareholders (HK\$ mn)	6,069	4,043	2,865	5,020	5,819
EPS (HK\$)	1.56	1.04	0.73	1.28	1.49
YoY growth (%)	6.6	(33.4)	(29.3)	75.2	15.9
P/E (x)	6.1	9.2	13.0	7.4	6.4
P/B (x)	0.74	0.76	0.76	0.72	0.68
Yield (%)	8.2	6.1	6.3	6.6	6.9
ROE (%)	12.3	8.2	5.8	10.0	10.9
Net gearing (%)	7.0	0.0	28.9	24.7	19.6

Source: Company data, CMBIS estimates

### BUY (Maintain)

Target Price	HK\$13.00
(Previous TP)	HK\$14.06
Up/Downside	+36.4%
Current Price	HK\$9.53

### Conglomerate Sector

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### Stock Data

Mkt Cap (HK\$ mn)	37,273
Avg 3 mths t/o (HK\$ mn)	29.11
52w High/Low (HK\$)	18.8 / 9.48
Total Issued Shares (mn)	3,911.1
Source: Bloomberg	

### Shareholding Structure

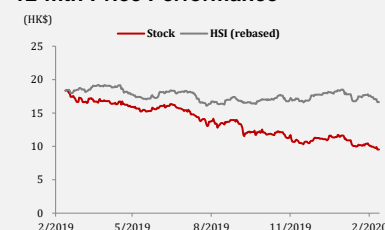
New World Development	60.86%
Source: HKEx	

### Share Performance

	Absolute	Relative
1-mth	-5.3%	-4.6%
3-mth	-9.2%	-8.5%
6-mth	-29.4%	-30.5%

Source: Bloomberg

### 12-mth Price Performance



Source: Bloomberg

### Auditor: PricewaterhouseCoopers

### Related Reports:

1. NWS Holdings (659 HK) – Impact of Toll Fee Exemption – 18 Feb 2020
2. NWS Holdings (659 HK) – Road to recovery – takeaways from tour – 21 Jan 2020
3. NWS Holdings (659 HK) – FTLife acquisition to drive earnings recovery – 5 Nov 2019
4. NWS Holdings (659 HK) – Results missed but worst is over – 26 Sep 2019
5. NWS Holdings (659 HK) – Initiation: Adding growth to defensive business – 19 Jul 2019

## 1H20 Results Review

Figure 1: 1H20 results review

Six months ended 31 Dec HK\$ mn	1H19	1H20	YoY %	CMBI 1H20E	Diff. % Beat / (Miss)	Remarks
Revenue	14,188	13,216	(7)	15,808	(16)	
Attributable Operating Profit (AOP)	2,432	2,290	(6)	2,713	(16)	Core Business slightly missed, while Facilities Mgmt was the main drag
Profit attributable to shareholders	2,274	1,514	(33)	1,631	(7)	Decrease magnified by one-off exceptional loss on disposal, increase in finance cost due to bond issuance, profit attributable to perpetual bondholders
EPS (HKD)	0.58	0.39	(34)	0.42	(7)	

Source: Company data, CMBIS estimates

Figure 2: Attributable Operating Profit (AOP) by segment

Six months ended 31 Dec							
HK\$ mn	1H19	1H20	YoY % Fav / (Unfav)	CMBI 1H20E	Diff. % Beat / (Miss)	Remarks	
Core Business	Roads	949	950	0	924	3	Contribution by 3 newly acquired roads; Excluding exchange rate effect, AOP would have +4%
	Aviation	232	268	16	351	(24)	Full period contribution from the acquisition of Sky Aviation; MTM loss of on interest rate swap
	Construction	655	670	2	684	(2)	Value of contracts on hand +36% YoY
	Insurance	-	160	N/A	195	(18)	FTLife acquisition completed in Nov 2019, contributed two-month AOP
	Sub-total	1,836	2,048	12	2,155	(5)	
Strategic Portfolio	Environment	450	233	(48)	269	(13)	Absence of one-off fair value gain of HK\$232.5mn from SUEZ NWS in 1H19
	Logistics	339	339	0	338	0	ATL Logistics Centre's average occupancy rate at 99.7%
	Facilities Mgmt.	(147)	(364)	(148)	(208)	(75)	Free Duty's loss widened
	Transport	(26)	(29)	(12)	(1)	(1,972)	Higher operating costs offset the bus fare increase
	Strategic Inv.	(19)	63	430	161	(61)	
	Sub-total	596	242	(59)	558	(57)	
Total AOP		2,432	2,290	(6)	2,713	(16)	

Source: Company data, CMBIS estimates

Figure 3: Earnings revision

HK\$ mn	New		Old		Change (%)		vs. Consensus (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Revenue	33,675	38,359	33,956	38,963	(1)	(2)	1	(2)
Attributable Operating Profit (AOP)	4,067	6,375	4,671	6,972	(13)	(9)	N/A	N/A
-Core Business AOP	3,750	5,420	3,733	5,612	0	(3)	N/A	N/A
-Strategic Portfolio AOP	351	966	938	1,360	(63)	(29)	N/A	N/A
Profit for the year	3,471	5,640	3,965	6,049	(12)	(7)	N/A	N/A
Profit attributable to shareholders	2,865	5,020	3,356	5,426	(15)	(7)	(26)	(9)
EPS (HKD)	0.73	1.28	0.86	1.39	(15)	(7)	(33)	(2)

Source: Company data, Bloomberg, CMBIS estimates

## COVID-19 delays earnings recovery

### Roads hit by drop in traffic flow and toll fee exemption policy

The COVID-19 outbreak is causing significant drop in Roads segment's AOP. Traffic flow all over China has slumped since mid-Jan, and then the Ministry of Transport (MoT) of the PRC issued the Notice on the implementation of the Toll Fee Exemption which took effect from 17 Feb 2020, until the end of the prevention and control measures taken by the government over COVID-19 (see our report [NWS Holdings \(659 HK\) – Impact of Toll Fee Exemption](#)).

MoT did state that it would consider launching “relevant ancillary protective measures to protect the rights of toll roads users, creditors, investors and operators”. 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.

### Facilities Mgmt under further pressure

Facilities Management (mainly HKCEC, Free Duty, Gleneagles Hospital HK) suffered from HK's social events in 1H20, and is under even more pressure in 2H20 due to COVID-19. To mitigate the negative impact, NWS discontinued Free Duty business in Macau and is streamlining its business and controlling costs (e.g. encourage staff to take no-pay leaves, negotiate rental concession with landlord).

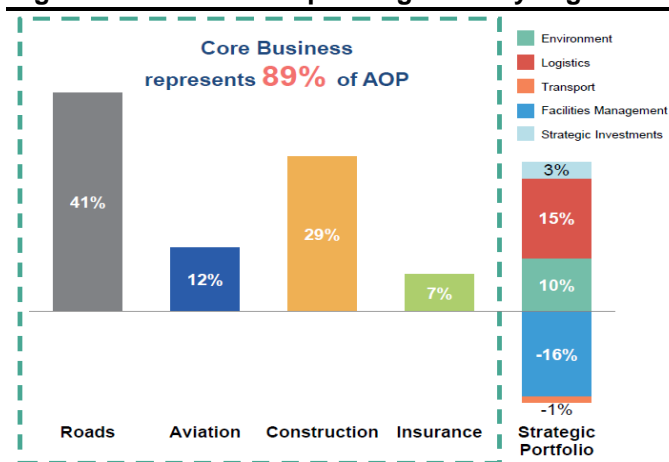
Aviation (aircraft leasing) has no immediate impact from COVID-19, as it has long remaining lease term averaging ~7 years. But in case the outbreak lasts for a long time, lessees might ask for rental concession.

## Valuation at trough

### Maintain BUY, TP cut to HK\$13.00

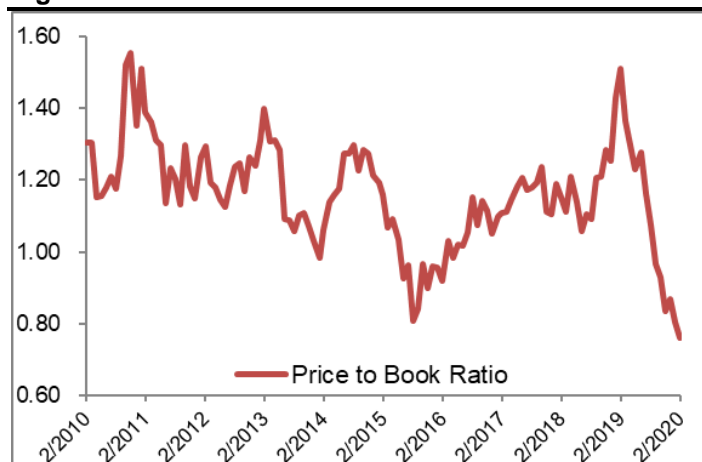
We revise FY20E AOP / EPS by -13% / -15%, and NAV by -1.1%. TP is cut from HK\$14.06 to HK\$13.00, based on 25% discount to FY20E NAV (vs. 20% before). A larger discount reflects lower economic forecasts of China & HK economic growth and wider discounts in other conglomerates' valuation. NWS's long-term fundamentals are intact. Trading at 0.76x P/B, a historical low, it remains an attractive yield play with 6.3% FY20E dividend yield.

Figure 4: Attributable Operating Profit by segment



Source: Company data

Figure 5: P/B at historical low



Source: Bloomberg, CMBIS estimates

Figure 6: NAV by sum-of-the-parts

	Valuation method	FY20E GAV (HK\$mn)	FY20E GAV per share (HK\$)	% of GAV
<b>Roads</b>		<b>20,954</b>	<b>5.36</b>	<b>22%</b>
Subsidiaries	DCF: WACC 7.0%	15,617	3.99	16%
Associates & JVs	P/E: 10x	5,337	1.36	6%
<b>Aviation (Goshawk)</b>	<b>P/E: 9x</b>	<b>5,149</b>	<b>1.32</b>	<b>5%</b>
<b>Construction</b>		<b>9,264</b>	<b>2.37</b>	<b>10%</b>
Construction	P/E: 8.5x	8,380	2.14	9%
Wai Kee	Market value: HK\$4.46/sh	883	0.23	1%
<b>Insurance</b>	<b>P/EV: 1.34x</b>	<b>22,083</b>	<b>5.65</b>	<b>23%</b>
<b>Environment</b>		<b>6,208</b>	<b>1.59</b>	<b>6%</b>
SUEZ NWS	P/E: 11x	3,036	0.78	3%
Derun Environment	Committed capital	2,072	0.53	2%
Power	P/E: 9x	1,100	0.28	1%
<b>Logistics</b>		<b>19,238</b>	<b>4.92</b>	<b>20%</b>
ATL Logistics Centre	Cap rate: 4.5%	17,039	4.36	18%
CUIRC	P/E: 11x	1,155	0.30	1%
Xiamen port	P/E: 10.2x	1,044	0.27	1%
<b>Facilities Management</b>		<b>7,740</b>	<b>1.98</b>	<b>8%</b>
HKCEC & Free Duty	DCF: WACC 6.2%	5,740	1.47	6%
Gleneagles Hospital HK	Committed capital	2,000	0.51	2%
<b>Transport</b>	<b>P/E: 8x</b>	<b>-511</b>	<b>-0.13</b>	<b>-1%</b>
<b>Strategic investments</b>	<b>Book value</b>	<b>9,360</b>	<b>2.39</b>	<b>10%</b>
Less Head office expense	P/E: 5x	(3,750)	(0.96)	-4%
Gross Asset Value (GAV)		95,733	24.48	
Less Net debt de facto		(27,962)	(7.15)	
<b>Net Asset Value (NAV)</b>		<b>67,771</b>	<b>17.33</b>	
Current discount to FY20E NAV	45%	Current share price	HK\$9.53	
<b>Target discount to FY20E NAV</b>	<b>25%</b>	<b>Target price</b>	<b>HK\$13.00</b>	

Source: Company data, CMBIS estimates

## Financial Summary

### Income statement

YE 30 Jun (HK\$ mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Revenue</b>	<b>35,115</b>	<b>26,834</b>	<b>33,675</b>	<b>38,359</b>	<b>39,850</b>
Roads	2,624	2,529	2,354	2,637	2,723
Construction	23,260	16,211	19,190	20,568	21,535
Aviation	161	162	-	-	-
Insurance	-	-	5,043	7,565	7,716
Facilities Management	5,571	4,152	3,267	3,593	3,773
Transport	3,499	3,780	3,821	3,996	4,102
Cost of sales	(31,332)	(23,791)	(29,641)	(32,689)	(33,876)
<b>Gross profit</b>	<b>3,783</b>	<b>3,043</b>	<b>4,034</b>	<b>5,671</b>	<b>5,974</b>
Other income/gains	2,809	1,030	500	500	500
General and administrative	(1,466)	(1,418)	(1,931)	(2,201)	(2,215)
<b>Operating profit</b>	<b>5,126</b>	<b>2,655</b>	<b>2,604</b>	<b>3,969</b>	<b>4,258</b>
Finance costs	(348)	(452)	(828)	(858)	(763)
Associated companies	756	759	613	1,062	1,326
JV	1,331	1,949	1,571	2,156	2,357
<b>Profit before income tax</b>	<b>6,866</b>	<b>4,911</b>	<b>3,960</b>	<b>6,330</b>	<b>7,179</b>
Income tax expenses	(745)	(652)	(490)	(690)	(736)
<b>Profit for the year</b>	<b>6,121</b>	<b>4,259</b>	<b>3,471</b>	<b>5,640</b>	<b>6,444</b>
Perpetual capital securities	-	(187)	(582)	(582)	(582)
Non-controlling interests	(52)	(29)	(23)	(38)	(43)
<b>Net profit to shareholders</b>	<b>6,069</b>	<b>4,043</b>	<b>2,865</b>	<b>5,020</b>	<b>5,819</b>

### Cash flow summary

YE 30 Jun (HK\$ mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Operating profit</b>	<b>5,126</b>	<b>2,655</b>	<b>2,604</b>	<b>3,969</b>	<b>4,258</b>
<b>Adjustments</b>					
Depreciation & amortization	1,487	1,482	1,443	1,481	1,520
Other non-cash items	(2,530)	(923)	(500)	(500)	(500)
<b>Working capital changes</b>					
Inventories	22	33	107	-	-
Trade & other receivables	(787)	360	(1,570)	(934)	(990)
Trade & other payables	859	(551)	2,394	794	842
Other items	983	(13)	(13)	(13)	(13)
<b>Net cash from operations</b>	<b>5,159</b>	<b>3,043</b>	<b>4,464</b>	<b>4,798</b>	<b>5,117</b>
Dividends from associates	542	485	613	1,062	1,326
Dividends from JV	1,845	1,888	1,571	2,156	2,357
Capital expenditures	(536)	(648)	(577)	(577)	(577)
Other investing activities	(344)	(5,240)	(22,217)	(1,639)	(1,639)
<b>Net cash from investing</b>	<b>1,507</b>	<b>(3,516)</b>	<b>(20,609)</b>	<b>1,003</b>	<b>1,468</b>
Change in borrowings	444	(159)	12,939	(2,000)	(2,000)
Dividends paid	(5,570)	(2,927)	(2,308)	(2,405)	(2,526)
Other financing activities	12	12,957	1,915	(425)	(425)
<b>Net cash from financing</b>	<b>(5,115)</b>	<b>9,871</b>	<b>12,547</b>	<b>(4,830)</b>	<b>(4,951)</b>
Net change in cash	821	8,473	(4,471)	(102)	516
Cash at the beginning of year	6,437	6,643	15,045	10,575	10,473
Currency translation diff.	39	(70)	-	-	-
<b>Cash at the end of year</b>	<b>7,297</b>	<b>15,045</b>	<b>10,575</b>	<b>10,473</b>	<b>10,989</b>

### Balance sheet

YE 30 Jun (HK\$ mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Non-current assets</b>	<b>55,507</b>	<b>56,580</b>	<b>112,442</b>	<b>112,652</b>	<b>113,125</b>
Property, plant & equip.	5,370	5,413	5,577	5,384	5,311
Intangible concession right	11,492	10,061	14,689	14,122	13,556
Associated companies	13,763	14,552	14,088	15,497	17,046
Joint ventures	15,008	13,645	13,530	13,395	13,261
Other non-current assets	9,874	12,908	64,559	64,255	63,951
<b>Current assets</b>	<b>19,267</b>	<b>29,485</b>	<b>38,743</b>	<b>40,161</b>	<b>42,290</b>
Cash and bank balances	6,657	15,059	10,575	10,473	10,989
Trade & other receivables	12,149	13,998	15,567	16,501	17,491
Other current assets	462	429	12,601	13,187	13,809
<b>Assets held-for-sale adj.</b>	<b>151</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Current liabilities</b>	<b>12,995</b>	<b>13,729</b>	<b>47,108</b>	<b>49,681</b>	<b>52,409</b>
Borrowings	1,035	2,403	3,366	3,366	3,366
Trade & other payables	11,384	10,843	13,236	14,031	14,872
Other current liabilities	576	483	30,506	32,285	34,171
<b>Non-current liabilities</b>	<b>11,807</b>	<b>15,089</b>	<b>43,851</b>	<b>40,196</b>	<b>36,675</b>
Borrowings	9,140	12,666	24,643	22,643	20,643
Debt securities	-	2,262	2,462	2,462	2,462
Other non-current liabilities	2,490	161	2,033	2,043	2,053
<b>Shareholders' funds</b>	<b>49,950</b>	<b>49,046</b>	<b>49,007</b>	<b>51,687</b>	<b>55,042</b>
Perpetual capital securities	-	8,040	10,529	10,529	10,529
Non-controlling interests	174	161	690	721	759
<b>Total equity</b>	<b>50,124</b>	<b>57,247</b>	<b>60,226</b>	<b>62,936</b>	<b>66,330</b>

### Key ratios

YE 30 Jun	FY18A	FY19A	FY20E	FY21E	FY22E
<b>AOP mix (%)</b>					
Roads	37.2	38.4	24.4	32.5	31.7
Construction	20.2	25.6	34.3	24.1	23.8
Aviation	13.3	10.6	14.1	10.4	10.4
Insurance	-	-	18.6	17.8	18.0
Environment	9.4	13.4	10.4	7.3	6.8
Logistics	12.5	13.8	15.8	10.3	9.6
Facilities Management	(1.4)	(8.4)	(19.1)	(4.7)	(2.7)
Transport	3.0	(0.2)	(1.6)	0.3	0.6
Strategic Investments	5.8	6.8	3.1	2.0	1.8
<b>P&amp;L ratios (%)</b>					
Operating margin	14.6	9.9	7.7	10.3	10.7
Net margin	17.3	15.1	8.5	13.1	14.6
<b>Balance sheet ratios</b>					
Current ratio (x)	1.48	2.15	0.82	0.81	0.81
Quick ratio (x)	1.45	2.12	0.82	0.80	0.80
Net debt / equity ratio (%)	7.0	0.0	28.9	24.7	19.6
<b>Returns (%)</b>					
ROE	12.3	8.2	5.8	10.0	10.9
ROA	7.9	4.9	2.4	3.3	3.8
<b>Per share (HK\$)</b>					
EPS	1.56	1.04	0.73	1.28	1.49
DPS	0.78	0.58	0.60	0.63	0.66
BVPS	12.8	12.6	12.5	13.2	14.1

Source: Company data, CMBIS estimates



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<b>SELL</b>	: Stock with potential loss of over 10% over next 12 months
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<b>OUTPERFORM</b>	: Industry expected to outperform the relevant broad market benchmark over next 12 months
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