

ENN Energy (2688 HK)

Share award scheme and shareholding increase plan bolster confidence amid conservative outlook

ENN remains conservative about the recovery of industrial gas sales in 2H23 and 2023. While its power plant gas sales are unlikely to recover and face customer structure adjustment, there is potential for partial gas sales recovery among other industrial gas users. We believe the dollar margin is expected to reach the full-year target. Recently, ENN has announced a share award scheme for employees and a shareholding increase plan by controlling shareholder Mr. Wang, showing confidence in the Company's development. **We trimmed TP to HK\$96.7, and maintained BUY due to an optimistic dollar margin and IE business expansion.**

- **ENN expected industrial gas sales recovery to remain conservative.** In 1H23, ENN reported an industrial gas sales loss of 1bn cbm, with 0.4bn cbm attributed to peak-shaving power plants in the coastal zone and the remaining 0.6bn cbm from industrial paper mills, factories, etc. The Company guided the recovery of gas sales from the power plants is unlikely in short to mid-term, but there is potential for partial gas sales recovery among other industrial gas users in 2H23 and beyond with the remaining 0.6bn cbm. The overall guidance for 2023 remains conservative. ENN is proactively addressing the situation by implementing active gas sales management measures internally and offering price incentives to attract more industrial gas users.
- **ENN's dollar margin is expected to reach the full-year target of RMB0.51cbm.** ENN's dollar margin improved to RMB0.52cbm in 1H23, driven by lower upstream gas costs, and active gas price pass-through implementation. With improved upstream supply and ongoing gas price pass-through, ENN will be well-positioned to navigate potential upstream cost fluctuation in winter and is expected to reach its target dollar margin of RMB0.51/cbm.
- **ENN announces share award scheme and shareholding increase plan, demonstrating confidence.** ENN has announced a share award scheme valued at up to US\$100mn. The scheme aims to recognize employee contributions, fostering an employee ownership mindset. Additionally, the Company has announced a shareholding increase plan by controlling shareholder Mr. Wang, highlighting confidence in ENN's operation and management's dedication to achieving strong business results in the future.
- **Trimmed TP to HK\$96.7, maintain BUY.** Based on our communication with the company, industrial gas sales recovery remained unfavourable due to client's structure adjustment and weak demand, and thus the retail gas sales guidance remains conservative for 2H23 and 2023. As a result, our C&I gas sales growth forecasts for 2023E/2024E/2025E are revised to -8.7%/0.3%/3.1% YoY. Revenue and net profit forecasts are adjusted accordingly. In addition, considering uncertainties in gas sales recovery, expected retail gas sales growth is revised from 10% YoY to 5% YoY (2024-26E) and 8% YoY to 4% YoY (2027-30E), leading to a SOTP DCF TP of HK\$96.7. We stay optimistic on ENN's dollar margin improvement and IE business expansion. Maintain BUY.

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	93,113	110,051	102,561	110,589	126,171
YoY growth (%)	30.0	18.2	(6.8)	7.8	14.1
Net profit (RMB mn)	7,755.0	5,865.0	6,420.2	7,861.8	8,671.0
YoY growth (%)	23.5	(24.4)	9.5	22.5	10.3
EPS (Reported) (RMB)	6.88	5.20	6.05	7.42	8.26
Consensus EPS (RMB)	na	5.20	6.74	7.43	8.06
P/E (x)	16.6	18.7	9.8	8.0	7.2
P/B (x)	3.6	2.8	1.5	1.4	1.3
ROE (%)	23.4	15.7	15.6	17.2	17.2

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price **HK\$96.70**
(Previous TP) HK\$123.60
Up/Downside **51.7%**
Current Price **HK\$63.75**

China Energy

Megan Xia, CESGA
(852) 3761 0836
meganxia@cmbi.com.hk

Stock Data

Mkt Cap (HK\$ mn)	72,115.2
Avg 3 mths t/o (HK\$ mn)	287.31
52w High/Low (HK\$)	124.29/53.85
Total Issued Shares (mn)	1,131

Source: FactSet

Shareholding Structure

Xinneng (Hong Kong) Energy Investment	33.4%
The Capital Group	12.8%

Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-20.3%	-20.5%
3-mth	-36.4%	-30.7%
6-mth	-38.1%	-32.5%

Source: FactSet

12-mth Price Performance



Source: FactSet

Figure 1: Revision table

	Old			New			Change(%)		
	2023E	2024E	2025E	2023E	2024E	2025E	2023E	2024E	2025E
Total gas sales volume (mcbm)	33,417	35,823	39,078	30,744	31,864	34,045	-8.0%	-11.1%	-12.9%
Retail gas sales volume (mcbm)	27,337	29,439	32,055	24,664	25,479	27,023	-9.8%	-13.5%	-15.7%
Residential connection (CTG incl. mm HH)	1.95	1.79	1.74	1.95	1.79	1.74	0.0%	0.0%	0.0%
Revenue (HK\$, mn)	108,556	119,935	136,911	105,231	110,589	126,171	-3.1%	-7.8%	-7.8%
Net Income (HK\$, mn)	7,811	9,125	9,881	6,324	7,862	8,671	-19.0%	-13.8%	-12.2%
EPS (HK\$)	7.25	8.54	9.33	5.96	7.42	8.26	-17.8%	-13.1%	-11.4%

Source: Company data, CMBIGM estimates

Figure 2: DCF traditional business valuation

DCF Valuation	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E	FY29E	FY30E	FY31E	FY32E
Key operating forecasts										
City gas sales volume (mcbm)	24,664	25,897	27,192	28,552	29,694	30,881	32,117	33,401	34,737	36,127
YoY change (%)	-4.9%	5.0%	5.0%	5.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%
Wholesale gas volume (mcbm)	6,080	6,384	6,704	7,039	7,320	7,613	7,918	8,234	8,564	8,906
YoY change (%)	-10.0%	5.0%	5.0%	5.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%
Annual residential connection	2.0	1.9	1.8	1.7	1.7	1.6	1.5	1.5	1.4	1.4
YoY change (%)	-6.3%	-4.0%	-4.0%	-4.0%	-4.0%	-4.0%	-4.0%	-4.0%	-4.0%	-4.0%
Accumulated residential customer	29.9	31.8	33.6	35.3	36.9	38.5	40.1	41.5	42.9	44.3
Turnover (HK\$ mn)	105,231	110,589	126,171	140,165	153,187	164,662	174,032	180,804	184,584	185,121
Turnover growth (%)	-4.4%	5.1%	14.1%	11.1%	9.3%	7.5%	5.7%	3.9%	2.1%	0.3%
EBIT (HK\$ mn)	10,445	12,557	13,851	14,687	16,204	17,583	18,758	19,668	20,264	20,508
EBIT margin	9.9%	11.4%	11.0%	10.5%	10.6%	10.7%	10.8%	10.9%	11.0%	11.1%
Tax rate	26.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
DD&A - HK\$ mn	2,886	3,174	3,459	3,843	4,200	4,515	4,772	4,957	5,061	5,076
CAPEX (HK\$ mn)	-13,207	-9,031	-9,035	-9,306	-9,585	-9,872	-10,169	-10,474	-10,788	-11,111
Invest in working capital	942	-751	1,636	-1,399	-1,302	-1,147	-937	-677	-378	-54
Free cash flow	-1,650	2,810	6,449	4,153	5,466	6,682	7,734	8,558	9,093	9,292
IE FCF	-989	-364	-140	28	553	1,168	1,890	2,633	3,914	4,549
Non IE FCF	-661	3,174	6,589	4,125	4,914	5,514	5,844	5,925	5179.63	4742.67
Years	1	2	3	4	5	6	7	8	9	10
Discount factor	0.93	0.86	0.80	0.74	0.69	0.64	0.59	0.55	0.51	0.47
Discount free cash flow	-613	2,732	5,263	3,057	3,379	3,518	3,460	3,255	2,640	2,243
Terminal value	81,449									
Terminal perpetual growth	2%									
Terminal EV/EBITDA(excl IE)	4.98									
Valuations (HK\$ mn)					WACC Calculations					
Terminal value				81,449	Cost of debt					4.0%
Terminal perpetual growth				2%	Tax rate					25.0%
Terminal EV/EBITDA				4.98	After tax cost of debt					3.0%
Total discount FCF				29,548	Cost of equity					9.8%
Discount terminal value				38,519	Adjusted beta					0.70
Firm value				68,067	Market risk premium					11.5%
Discount FCF(% of total)				56.6%	Risk free rate					1.8%
Terminal value (% of total)				43.4%	% of debt financing					30.0%
Add: Cash & cash equivalent				1,352	WACC					7.8%
Less: Debt				19,129						
Non-controlling interest				6,876						
Equity Value - (RMB, mn)				43,414						
Number of shares				1,126						
Share fair value (RMB)				38.54						
Share fair value (HK\$)				43.30						

Source: Company data, CMBIGM estimates

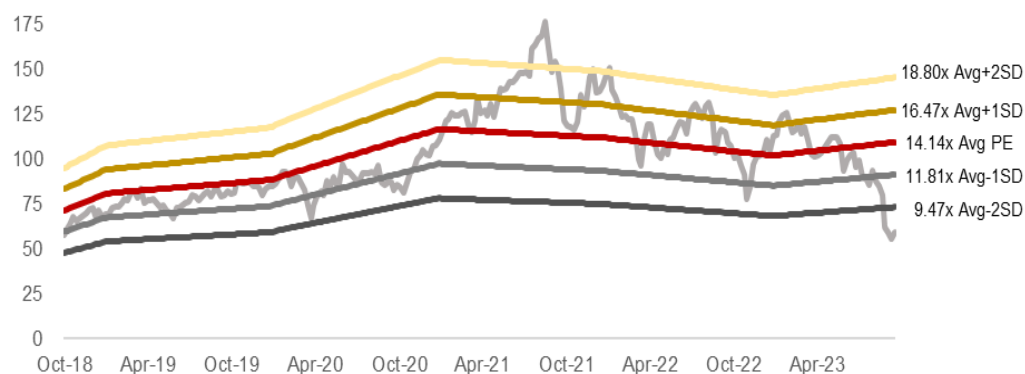
Figure 3: DCF traditional business valuation**SOTP Valuation**

Traditional business value - RMB	38.54
IE value - RMB	47.53
ENN's Total value	86.07
FX rate HK/RMB	0.89
Target price - HK\$	96.70

Source: Company data, CMBIGM estimates

Figure 4: PE Band

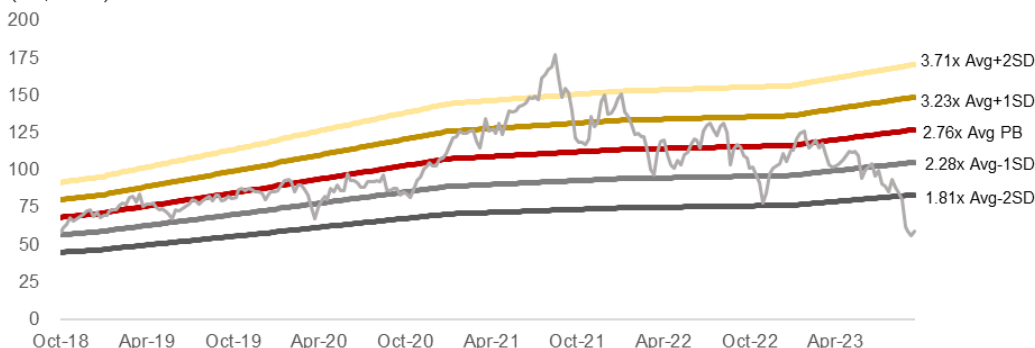
(HK\$/share)



Source: Company data, CMBIGM estimates

Figure 5: PB Band

(HK\$/share)



Source: Company data, CMBIGM estimates

Figure 6: Peers table

Company	Ticker	Closing Price (HK\$)	Mkt cap (HK\$mn)	EPS				PER			PBR		
				23E	24E	25E	CAGR	23E	24E	25E	23E	24E	25E
ENN ENERGY	2688 HK	63.75	72115.24	6.74	7.42	8.04	9.2%	8.83	8.03	7.41	1.52	1.34	1.19
TIAN LUN GAS HOL	1600 HK	3.56	3495.51	0.66	0.75	0.88	15.6%	5.05	4.43	3.78	0.60	0.49	0.44
CHINA GAS HOLDIN	384 HK	7.64	41527.78	1.14	1.09	1.22	3.4%	6.70	7.02	6.26	0.62	0.66	0.63
CHINA RES GAS	1193 HK	22.50	52065.29	2.50	2.68	2.95	8.6%	9.01	8.40	7.64	1.20	1.09	1.01
TOWNGAS SMART EN	1083 HK	3.28	11002.76	0.45	0.51	0.50	5.7%	7.27	6.50	6.51	0.48	0.46	0.44
KUNLUN ENERGY	135 HK	6.72	58187.15	0.75	0.83	0.91	10.1%	8.40	7.54	6.94	0.84	0.78	0.72
Average								7.5	7.0	6.4	0.9	0.8	0.7

Source: Company data, CMBIGM estimates

Financial Summary

INCOME STATEMENT	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Revenue	71,617	93,113	110,051	102,561	110,589	126,171
Cost of goods sold	(59,285)	(79,057)	(94,295)	(87,410)	(93,395)	(106,204)
Gross profit	12,332	14,056	15,756	15,151	17,194	19,968
Operating expenses	(4,181)	(4,847)	(5,441)	(5,333)	(5,972)	(7,444)
Selling expense	(951)	(1,122)	(1,180)	(1,128)	(1,327)	(1,640)
Admin expense	(3,230)	(3,725)	(4,261)	(4,205)	(4,645)	(5,804)
Operating profit	16,513	18,903	21,197	20,484	23,166	27,412
Other income	952	1,077	953	1,132	1,209	1,264
Other gains/(losses)	282	984	(1,569)	(400)	(550)	(700)
Share of (losses)/profits of associates/JV	782	699	25	25	676	764
EBITDA	12,248	14,228	12,319	13,461	15,731	17,311
Depreciation	2,081	2,259	2,595	2,886	3,174	3,459
EBIT	10,167	11,969	9,724	10,574	12,557	13,851
Interest income	(609)	(576)	(672)	(700)	(750)	(800)
Pre-tax profit	9,558	11,393	9,052	9,874	11,807	13,051
Income tax	(2,227)	(2,398)	(2,388)	(2,567)	(2,952)	(3,263)
After tax profit	7,331	8,995	6,664	7,307	8,855	9,789
Minority interest	1,053	1,240	799	887	993	1,117
Discontinued operations	6,278	7,755	5,865	6,420	7,862	8,671
Net profit	6,278	7,755	5,865	6,420	7,862	8,671

BALANCE SHEET	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Current assets	23,568	27,558	27,133	20,230	21,361	26,900
Cash & equivalents	8,630	8,684	8,056	998	854	3,683
Restricted cash	116	363	458	230	240	249
Account receivables	9,053	10,568	10,675	11,036	11,901	13,581
Inventories	1,285	1,508	1,708	1,846	1,991	2,271
Prepayment	0	0	0	0	0	0
Financial assets at FVTPL	406	1,737	1,488	1,488	1,488	1,488
Other current assets	3,346	3,923	4,110	4,202	4,531	5,170
Contract assets	732	775	638	430	357	458
Non-current assets	66,475	72,430	75,218	85,861	91,969	97,932
PP&E	41,861	46,793	50,380	59,188	64,214	68,905
Right-of-use assets	2,129	2,119	2,323	2,305	2,387	2,463
Deferred income tax	1,370	1,212	1,557	1,949	2,101	2,397
Investment in JVs & assos	7,760	8,718	8,477	10,285	11,168	12,116
Intangibles	4,446	4,311	4,549	3,973	3,785	3,585
Goodwill	2,511	2,520	2,520	2,760	2,880	3,000
Financial assets at FVTPL	5,052	5,352	4,327	4,327	4,327	4,327
Other non-current assets	1,346	1,405	1,085	1,075	1,106	1,138
Total assets	90,043	99,988	102,351	106,091	113,329	124,832
Current liabilities	33,233	41,579	36,082	37,612	39,061	43,504
Short-term borrowings	4,590	6,150	6,341	7,561	7,893	8,225
Account payables	8,302	10,172	8,066	11,543	12,449	14,202
Tax payable	971	909	1,517	1,099	1,237	1,381
Other current liabilities	5,039	9,365	4,657	4,186	4,474	4,950
Lease liabilities	89	75	91	91	91	91
Contract liabilities	14,242	14,908	15,410	13,132	12,916	14,655
Non-current liabilities	20,638	16,259	20,714	18,290	19,065	20,502
Long-term borrowings	3,212	2,993	2,825	2,440	2,400	2,723
Convertible bonds	0	0	0	0	0	0
Obligations under finance leases	0	0	0	0	0	0
Deferred income	2,562	2,785	2,974	3,077	3,318	3,785
Other non-current liabilities	14,864	10,481	14,915	12,774	13,348	13,994
Total liabilities	53,871	57,838	56,796	55,902	58,126	64,005
Share capital	117	117	117	118	118	118
Other reserves	30,444	35,660	38,917	43,196	47,813	52,989
Total shareholders equity	30,561	35,777	39,034	43,313	47,930	53,106
Minority interest	5,611	6,373	6,521	6,876	7,273	7,720
Total equity and liabilities	90,043	99,988	102,351	106,091	113,329	124,832

CASH FLOW	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	9,558	11,393	9,052	9,874	11,807	13,051
Depreciation & amortization	2,081	2,259	2,595	2,886	3,174	3,459
Tax paid	(1,554)	(2,079)	(1,936)	(3,275)	(2,725)	(2,947)
Change in working capital	(208)	187	(1,539)	550	(359)	1,636
Others	(181)	(3)	(1,285)	1,065	(885)	(998)
Net cash from operations	9,696	11,756	6,888	11,102	11,013	14,202
Investing						
Capital expenditure	(3,906)	(4,932)	(3,587)	(8,808)	(5,026)	(4,691)
Others	(2,892)	(2,812)	(4,732)	(4,498)	(4,114)	(4,463)
Net cash from investing	(6,798)	(7,744)	(8,319)	(13,306)	(9,140)	(9,154)
Financing						
Dividend paid	(1,688)	(2,290)	(2,004)	(2,178)	(3,281)	(3,531)
Net borrowings	388	3,599	(5,383)	830	830	830
Others	(3,061)	(1,777)	(2,460)	(1,787)	(2,847)	(3,048)
Net cash from financing	(2,673)	1,822	(7,843)	(957)	(2,017)	(2,218)
Net change in cash						
Cash at the beginning of the year	7,373	7,598	13,433	4,159	998	854
Others	(7,148)	(1,763)	(22,707)	(7,321)	(1,142)	1,976
Cash at the end of the year	225	5,835	(9,274)	(3,161)	(144)	2,830
GROWTH	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Revenue	2.0%	30.0%	18.2%	(6.8%)	7.8%	14.1%
Gross profit	9.5%	14.0%	12.1%	(3.8%)	13.5%	16.1%
Operating profit	7.6%	14.5%	12.1%	(3.4%)	13.1%	18.3%
EBITDA	7.9%	16.2%	(13.4%)	9.3%	16.9%	10.0%
EBIT	6.3%	17.7%	(18.8%)	8.7%	18.7%	10.3%
Net profit	10.7%	23.5%	(24.4%)	9.5%	22.5%	10.3%
PROFITABILITY	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Gross profit margin	17.2%	15.1%	14.3%	14.8%	15.5%	15.8%
Operating margin	23.1%	20.3%	19.3%	20.0%	20.9%	21.7%
EBITDA margin	17.1%	15.3%	11.2%	13.1%	14.2%	13.7%
Return on equity (ROE)	22.3%	23.4%	15.7%	15.6%	17.2%	17.2%
GEARING/LIQUIDITY/ACTIVITIES	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Current ratio (x)	0.7	0.7	0.8	0.5	0.5	0.6
Receivable turnover days	10.6	10.9	11.2	11.1	10.7	na
Inventory turnover days	10.6	10.9	11.2	11.1	10.7	na
Payable turnover days	68.6	72.0	63.4	61.1	67.2	na
VALUATION	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
P/E	14.4	16.6	18.7	9.8	8.0	7.2
P/B	3.0	3.6	2.8	1.5	1.4	1.3

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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SELL : Stock with potential loss of over 10% over next 12 months
NOT RATED : Stock is not rated by CMBIGM

OUTPERFORM : Industry expected to outperform the relevant broad market benchmark over next 12 months
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UNDERPERFORM : Industry expected to underperform the relevant broad market benchmark over next 12 months

CMB International Global Markets Limited

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

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