

# China Gas Holdings (384 HK)

## Earnings growth to accelerate with extensive M&A and southern heating projects

CGH placed 392mn new shares for HK\$11.6bn on 22 April. The placement was priced at HK\$29.75, representing 9% discount to closing price prior to the placement date. The market took a cautious view for the placement purpose and the fundraising timing, which could explain CGH's recent share price softness. Following the completion of the placement, CGH announced indirect acquisition of 49% shares in Beijing Huayou United Gas on 2 May, reflecting CGH's strong execution capability again. We remain positive on CGH, and believe the recent share price retreat created good timing to accumulate the share. Maintain BUY with TP slightly trimmed to HK\$34.82.

- **Raised HK\$11.6bn through 392mn new share placement.** According to our discussion with CGH, the Company planned to use proceeds with 1) 40% for acquisition of city gas project; 2) 25% for expansion of LPG Smart MicroGrid business; 3) 25% for development of distributed heating business; and 4) 10% for replenishment of working capital. We expect CGH's earnings growth to accelerate shortly on the back of new funding support.
- **Acquiring Beijing Huayou at 7x FY20 PER.** CGH announced to indirectly acquire 49% shares of Beijing Huayou United Gas Development Co., Ltd. (Beijing Huayou, 北京华油联合燃气开发有限公司) for consideration of RMB484mn. Beijing Huayou owns several gas distribution projects in Beijing, Shandong, and Liaoning. In 2020, Beijing Huayou and affiliates realized a natural gas sales volume of 630mcbm and a net profit of RMB140mn. The consideration represents 7.1x FY22E PER, less than CGH's current valuation (11.4x FY22E PER), which will enhance CGH's EPS and boost overall valuation, in our view. Mgmt. expect the project to have a 9-month profit contribution in FY22E. We expect more acquisition announcements in the coming 6-12 months.
- **Distributed heating: a new growth engine.** We observed that CGH had accelerated distributed gas heating development in Central and Eastern China from 2021E (Fig. 1-4). We think distributed gas heating is a consumption upgrade from basic residential gas distribution services, and the business can break through concession operating areas and penetrate into other gas distributors' hinterland. CGH aims at distributed heating connection market and VAS opportunities through heating radiator sales. According to our preliminary discussion with the Company, CGH intends to develop 20-30mn sq m distributed gas heating areas in FY22E. We believe the fundraising through placement will help CGH seize the market.

### Earnings Summary

(YE 31 Mar)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue (HK\$ mn)	59,386	59,540	66,999	80,020	93,045
YoY growth (%)	12.4	0.3	12.5	19.4	16.3
Net income (HK\$ mn)	8,224	9,188	10,669	13,302	15,770
EPS (HK\$)	1.63	1.76	2.05	2.46	2.75
YoY growth (%)	32.7	8.2	16.2	20.2	11.9
Consensus EPS (HK\$)	n/a	n/a	2.06	2.38	2.65
P/E (x)	17.2	15.9	13.7	11.4	10.2
P/B (x)	4.1	3.7	3.1	2.3	2.0
Yield (%)	1.6	1.8	2.1	2.5	2.8
ROE (%)	24.1	23.2	22.4	20.0	20.0
Net gearing (%)	69.1	81.5	68.9	21.6	10.1

Source: Company data, Bloomberg, CMBIS estimates

**BUY (Maintain)**

Target Price **HK\$34.82**  
 (Previous TP **HK\$37.12**)  
 Up/Downside **+24.4%**  
 Current Price **HK\$28.00**

### China Gas Distributor

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### Stock Data

Mkt Cap (HK\$ mn)	156,922
Avg 3 mths t/o (HK\$ mn)	497.35
52w High/Low (HK\$)	35/20.43
Total Issued Shares (mn)	5,604

Source: Bloomberg

### Shareholding Structure

Beijing Enterprise	22.1%
Liu Minghui	12.9%
Chiu Tat Jung	10.8%
Free float	47.1%

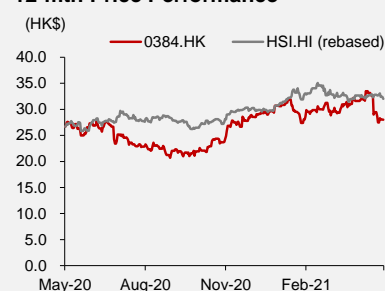
Source: HKEx

### Share Performance

	Absolute	Relative
1-mth	-11.4%	-9.6%
3-mth	-2.1%	1.2%
6-mth	15.4%	1.5%
12-mth	-0.2%	-13.3%

Source: Bloomberg

### 12-mth Price Performance



Source: Wind

**Auditor: Deloitte**

### Related Reports

1. China Gas Sector – City Gas 3.0: Differentiating Growth Paths – 8 Dec 2020
2. China Gas Holdings (384 HK) – Outstanding 1HFY21 performance – 30 Nov 2020
3. China Gas Holdings (384 HK) – initiation) – LPG micro grid: a new growth engine – 29 Jun 2020

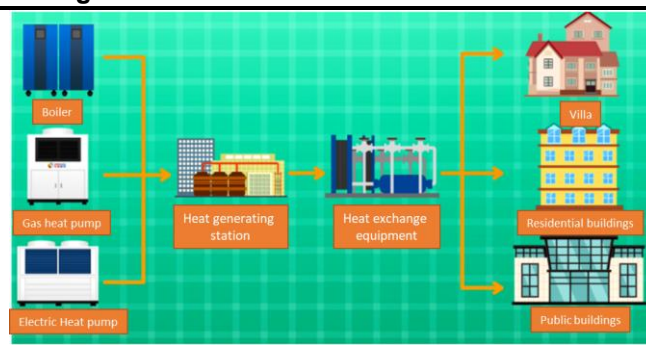
- **Earnings growth to accelerate in FY22E.** FY22E will be the first option exercising year with the condition of adjusted net profit reaching HK\$14bn. We expect CGH to spurt for the earning condition, supported by abundant funding, and opportunities from project acquisition, LPG Smart MicroGrid, and distributed heating business. Once the condition is achieved, it will reflect ~30% net profit growth in FY22E.
- **Maintain BUY with TP trimmed slightly to HK\$34.82.** We cut CGH's TP slightly by 6.2% to HK\$34.82 to mainly reflect share dilution impact from the placement. With share price decline of 8.8% YTD, CGH is the worst performing gas distributor under our coverage. We think the market is overly worried about the placement and its potential impacts. Trading at 11.4x FY22E PER, we think CGH's valuation is attractive. We believe the recent share price retreat creates a good entry point. Maintain BUY.

**Figure 1: CGH's residential heating campaign in Central China**



Source: Company data, CMBIS

**Figure 2: CGH's residential heating business is not limited to gas heating, and is able to penetrate other gas distributors' concession areas**



Source: Company data, CMBIS

**Figure 3: CGH is charging RMB150/sq m for heating radiator installation in Zaoyang City**



Source: Company data, CMBIS

**Figure 4: CGH is charging RMB170/sq m for floor heating installation in Zaoyang City**



Source: Company data, CMBIS

**Figure 5: Earnings revision**

	Old			New			Change(%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Total gas sales volume (mcbm)	28,927	33,642	38,558	28,927	33,642	38,558	0.0%	0.0%	0.0%
Retail gas sales volume (mcbm)	18,808	23,017	27,402	18,808	23,017	27,402	0.0%	0.0%	0.0%
Residential connection (CTG incl. mm HH)	5.71	5.95	6.12	5.71	5.95	6.12	0.0%	0.0%	0.0%
Revenue (HK\$, mn)	66,999	80,020	93,045	66,999	80,020	93,045	0.0%	0.0%	0.0%
Net Income (HK\$,mn)	10,668	13,204	15,566	10,669	13,302	15,770	0.0%	0.7%	1.3%
EPS (HK\$)	1.97	2.35	2.73	2.05	2.46	2.75	0.0%	0.7%	1.3%

Source: CMBIS estimates

## Financial Summary

### Income statement

YE 31 Mar (HK\$ mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Revenue</b>	<b>59,386</b>	<b>59,540</b>	<b>66,999</b>	<b>80,020</b>	<b>93,045</b>
<b>Costs of sales</b>	<b>(45,327)</b>	<b>(42,443)</b>	<b>(47,773)</b>	<b>(56,582)</b>	<b>(65,899)</b>
<b>Gross profit</b>	<b>14,059</b>	<b>17,097</b>	<b>19,226</b>	<b>23,438</b>	<b>27,146</b>
Other income	786	640	710	941	1,326
Other gains and losses	295	(180)	50	50	50
Selling and distribution costs	(1,820)	(1,973)	(2,187)	(2,572)	(2,944)
Administrative expenses	(2,442)	(2,447)	(2,720)	(3,208)	(3,684)
Profit from associates	520	405	565	629	702
Profit from JVs	1,132	571	625	613	637
Share-based payments	(63)	-	(50)	(50)	(50)
<b>EBIT</b>	<b>12,467</b>	<b>14,113</b>	<b>16,220</b>	<b>19,841</b>	<b>23,183</b>
Finance costs	(1,284)	(1,388)	(1,411)	(1,529)	(1,615)
<b>Pre-tax profit</b>	<b>11,183</b>	<b>12,725</b>	<b>14,809</b>	<b>18,312</b>	<b>21,568</b>
Income tax	(2,198)	(2,464)	(2,962)	(3,662)	(4,314)
Less: Minority interests	(760)	(1,072)	(1,179)	(1,348)	(1,484)
<b>Net profit</b>	<b>8,224</b>	<b>9,188</b>	<b>10,669</b>	<b>13,302</b>	<b>15,770</b>

### Cash flow summary

YE 31 Mar (HK\$ mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Pre-tax profit</b>	<b>11,183</b>	<b>12,725</b>	<b>14,809</b>	<b>18,312</b>	<b>21,568</b>
D&A	1,326	1,591	1,910	2,203	2,495
Change in working capital	7,038	(8,091)	1,337	4,624	2,877
Taxation	(1,874)	(2,245)	(3,093)	(3,337)	(4,011)
Others	(7,556)	(1,001)	(145)	(275)	(175)
<b>Net cash from operating</b>	<b>10,117</b>	<b>2,979</b>	<b>14,817</b>	<b>21,527</b>	<b>22,754</b>
Capex & investments	(11,816)	(5,989)	(12,228)	(10,969)	(11,016)
Others	784	(950)	-	-	-
<b>Net cash from investing</b>	<b>(11,032)</b>	<b>(6,939)</b>	<b>(12,228)</b>	<b>(10,969)</b>	<b>(11,016)</b>
Equity raised	3,785	(3)	(0)	11,604	-
Change of Debts	5,526	1,790	4,158	2,755	2,288
Dividend paid	(2,172)	(2,934)	(3,196)	(4,168)	(4,943)
Others	(804)	(1,100)	-	-	-
<b>Net cash from financing</b>	<b>6,335</b>	<b>(2,246)</b>	<b>962</b>	<b>10,191</b>	<b>(2,656)</b>
<b>Net change in cash</b>	<b>5,419</b>	<b>(6,207)</b>	<b>3,552</b>	<b>20,749</b>	<b>9,082</b>
Cash at the beginning of the year	8,246	13,239	7,119	10,671	31,419
Exchange difference	(427)	(450)	-	-	-
<b>Cash at the end of the year</b>	<b>13,239</b>	<b>6,582</b>	<b>10,671</b>	<b>31,419</b>	<b>40,501</b>
<b>Cash at balance sheet</b>	<b>13,239</b>	<b>7,119</b>	<b>10,671</b>	<b>31,419</b>	<b>40,501</b>

### Balance sheet

YE 31 Mar (HK\$ mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Non-current assets</b>	<b>68,277</b>	<b>72,558</b>	<b>82,851</b>	<b>91,626</b>	<b>100,160</b>
Investment properties	556	524	566	571	571
PPE	42,965	46,128	55,163	62,291	69,114
Prepaid lease payments	2,148	2,458	2,673	2,958	3,215
Investment in associates	5,746	7,063	7,628	8,258	8,960
Investment in JVs	8,022	7,815	7,963	8,606	9,273
Others non-current assets	8,840	8,570	8,858	8,943	9,028
<b>Current assets</b>	<b>41,603</b>	<b>39,509</b>	<b>44,771</b>	<b>65,286</b>	<b>74,984</b>
Inventories	3,412	3,246	3,653	4,203	4,701
Amount due from customers	-	-	-	-	-
Contract assets	7,185	12,751	12,146	9,434	7,301
Trade receivables	10,061	9,893	11,657	13,609	15,824
Bank balances and cash	13,239	7,119	10,671	31,419	40,501
Other current assets	7,706	6,500	6,645	6,621	6,657
<b>Current liabilities</b>	<b>46,644</b>	<b>49,347</b>	<b>47,324</b>	<b>49,947</b>	<b>53,703</b>
Trade and other payables	23,699	17,700	19,109	21,501	23,065
Amount due to customers	-	-	-	-	-
Contract liabilities	5,168	5,998	6,816	7,815	8,780
Taxation	1,245	1,246	1,333	1,648	1,941
Bank and other borrowings	16,408	24,121	19,773	18,679	19,604
Other current liabilities	125	282	293	303	314
<b>Non-current liabilities</b>	<b>22,453</b>	<b>16,936</b>	<b>25,273</b>	<b>29,182</b>	<b>30,605</b>
Borrowings	21,491	15,568	24,073	27,923	29,285
Deferred income tax	962	1,368	1,200	1,260	1,320
<b>Total net assets</b>	<b>40,782</b>	<b>45,783</b>	<b>55,025</b>	<b>77,784</b>	<b>90,836</b>
<b>Minority Interest</b>	<b>5,461</b>	<b>6,178</b>	<b>7,357</b>	<b>8,705</b>	<b>10,189</b>
<b>Shareholders' equity</b>	<b>35,321</b>	<b>39,605</b>	<b>47,667</b>	<b>69,079</b>	<b>80,647</b>

### Key ratios

YE 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Sales mix (%)</b>					
Sales of piped gas	45.6	45.4	49.5	50.5	51.6
Gas connection	21.0	23.0	21.2	18.5	16.2
Sales of LPG	26.8	23.1	17.7	17.5	16.7
Value-added service	6.6	8.4	11.6	12.1	13.1
Others	-	-	-	1.4	2.4
<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	21.0	23.7	24.2	24.8	24.9
Pre-tax margin	18.8	21.4	22.1	22.9	23.2
Net margin	13.8	15.4	15.9	16.6	16.9
Effective tax rate	19.7	19.4	20.0	20.0	20.0
<b>Balance sheet ratios</b>					
Current ratio (x)	0.89	0.80	0.95	1.31	1.40
Quick ratio (x)	9.7	10.2	11.5	13.0	14.4
Cash ratio (x)	0.3	0.2	0.2	0.6	0.8
Inventory turnover days	19.9	20.4	18.8	17.9	17.5
Receivable turnover days	58.6	61.2	58.7	57.6	57.7
Payable turnover days	152	178	141	131	123
Total debt / equity ratio (%)	92.9	87.2	80.2	60.3	54.2
Net debt / equity ratio (%)	69.1	81.5	68.9	21.6	10.1
<b>Returns (%)</b>					
ROE	24.1	23.2	22.4	20.0	20.0
ROA	7.5	8.2	8.4	8.5	9.0
<b>Per share</b>					
EPS (HK\$)	1.63	1.76	2.05	2.46	2.75
DPS (HK\$)	0.44	0.50	0.58	0.70	0.78
BVPS (HK\$)	6.77	7.60	9.15	12.33	13.8

Source: Company data, CMBIS estimates



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