

## Environmental Sector

### Monthly Insights: Positive surprise from the official 13<sup>th</sup> FYP on MWT and WWT sectors



- ❖ 13th FYP on MWT and WWT should boost >Rmb800bn investment
- ❖ Further implementation set up for soil pollution treatment
- ❖ Sector view: Start to focus on counters with potential high earnings growth in FY16

● **Official 13th FYPs on WWT and MWT to bring Rmb816bn new investment:** The 13th FYPs for both wastewater treatment (WWT) and municipal waste treatment (MWT) were announced on 23rd Jan. Capex for both 13th FYPs totaled Rmb816bn. In our view, WWT operators could potentially benefit from the revision of tariff as technical upgrade is estimated to be one of the key investments during the 13<sup>th</sup> FYP period. It is estimated that 42.2mt/day (~18% of the 2015-end total WWT capacity) will need to complete technical upgrade during the period. On the other hand, we expect WTE operators to continue competing for new projects, given the revised-up incineration capacity target by 2020 and accelerating development in WTE projects, especially in regions with relatively high growth (e.g. Guangdong, Anhui, Sichuan, etc).

● **New framework set up by MEP for soil remediation:** The MEP issued *Administrative Measures for Soil Environment of Polluted Land Pieces* ("Document"), which will be effective on July 2017. The Document has clarified: (i) the types of pollution and definition of polluted land piece; (ii) the responsible parties for soil pollution; (iii) survey and risk management on soil pollution; (iv) treatment and remediation; and (v) supervision and management. Following the announcement of Action Plan on Soil Pollution Control and Prevention, the Document provides the framework for soil pollution remediation and management. This could help speed up the treatment of soil pollution at the local government level, in our view.

● **Company updates:** Yunnan Water set up a new JV for solid waste treatment. Canvest signed a new strategic agreement to explore new business opportunities in Guangdong Province.

● **Start focusing on counters with potential high FY16 earnings growth:** The HK environmental sector advanced 3% MoM in Jan 2017, following the rebound of the general market. BEWG (371.HK; Buy), our top pick last month, surged 6.2% MoM. China Everbright (257.HK; NR) also surged 8.2% MoM, supported by the upbeat investment amount and overall planning of the 13<sup>th</sup> FYP on municipal waste treatment. Meanwhile, Beijing Origin Water (300070.CH; NR) declined 11.3% MoM as its FY16 earnings estimate announced by the company was slightly lower than expected. Looking forward, the results season for FY16 will start soon. Within the HK environmental sector, we suggest that investors start paying attention to counters likely to report high earnings growth in FY16. For instance, we estimate Canvest (1381.HK; Buy) to register 45% YoY net profit growth for FY16, mainly driven by construction revenue from new projects during 2H16. Yunnan Water (6839.HK; Buy) is another counter with high earnings growth in FY16. We estimate the counter to register 37% YoY growth in net profit, given the consistent contribution from both operational and construction revenues from new projects.

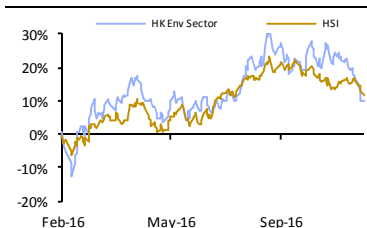


#### Sector Valuation (HK)

	(X)
FY16E avg P/E	14.8
FY17E avg P/E	11.7
FY16E avg P/B	2.1
FY17E avg P/B	1.8

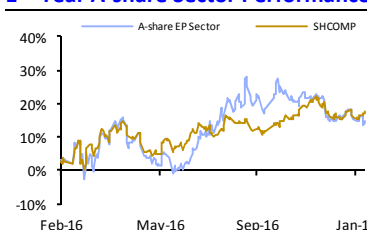
Source: Bloomberg, BOCOM Int'l

#### 1 – Year HK Sector Performance



Source: Bloomberg, BOCOM Int'l

#### 1 – Year A-share Sector Performance



Source: Bloomberg, BOCOM Int'l

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## Key Updates on Policy and Industries

- Official 13th FYPs on WWT and MWT to bring Rmb816bn new investment:** The 13th FYPs for both wastewater treatment (WWT) and municipal waste treatment (MWT) were announced on 23rd Jan. Capex for both 13th FYPs totaled Rmb816bn. Compared with the previous consultation drafts, we found that: (1) both target capex and incineration capacity were revised up by 30.9% and 13.6% in the official MWT 13<sup>th</sup> FYP, respectively; and (2) the 2020- end WWT capacity was lifted by 9.1% to 267.66mt/day, while the overall capex was lowered by 3.2% in the official WWT 13<sup>th</sup> FYP.

(Source: [http://www.gov.cn/zhengce/content/2016-12/05/content\\_5143290.htm](http://www.gov.cn/zhengce/content/2016-12/05/content_5143290.htm))

**Our comments:** In our view, WWT operators could potentially benefit from the revision of tariff as technical upgrade is estimated to be one of the key investments during the 13<sup>th</sup> FYP period. It is estimated that 42.2mt/day (~18% of the 2015-end total WWT capacity) will need to complete technical upgrade during the period. On the other hand, we expect WTE operators to continue competing for new projects, given the revised-up incineration capacity target by 2020 and accelerating development in WTE projects, especially in regions with relatively high growth (e.g. Guangdong, Anhui, Sichuan, etc).

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(Source: [http://www.mep.gov.cn/gkml/hbb/bl/201701/t20170118\\_394953.htm](http://www.mep.gov.cn/gkml/hbb/bl/201701/t20170118_394953.htm))

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**Figure 1: Other important news on the industry and policies**

Event	Summary	Source
MoF announced managing methods for PPP information platform	<ul style="list-style-type: none"> <li>The document gave guidelines on disclosure timing and the content required to be disclosed on PPP projects released in the centralized database.</li> </ul>	<a href="http://jrs.mof.gov.cn/zhengwuxinx/zhengcefabu/201701/t20170124_2526998.html">http://jrs.mof.gov.cn/zhengwuxinx/zhengcefabu/201701/t20170124_2526998.html</a>
President Xi reiterated the importance of ecological environment of Yangtze River	<ul style="list-style-type: none"> <li>President Xi stated local governments should prioritize environmental protection in the Yangtze River region over development plan.</li> </ul>	<a href="http://www.h2o-china.com/news/252981.html">http://www.h2o-china.com/news/252981.html</a>

Source: Various sources, BOCOM Int'l

## Company news and updates

- **BEWG (371.HK; Buy)** – BEWG has just announced the disposal of its entire stake (60%) in its Dalian subsidiary Bei Kong (Dalian) Investment Company at Rmb1.5bn. The purchaser of the 60% stake, Mr. Wu Lizhong, was originally the minority shareholder of the Dalian subsidiary. Upon the completion of the disposal, BEWG is expected to record a gain of HK\$7.8m before tax. BEWG indicated that the disposal was mainly due to: (1) corporate restructuring after BEWG has established its own business platform in Northeastern China; and (2) realizing its investment in the subsidiary at a fair value and using the proceeds for development of core businesses. We view the disposal as positive to BEWG, given the net proceeds could help further lower BEWG's net gearing in 2017E. Maintain Buy on BEWG.

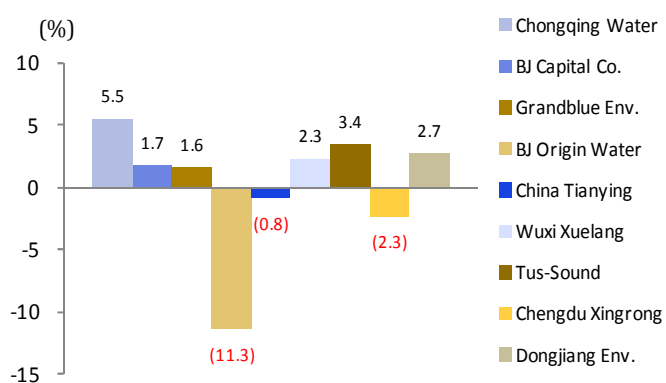
- **Yunnan Water (6839.HK; Buy)** – YNW formed a JV with Yunnan Sidu Investment Management to invest in solid waste treatment. YNW will inject Rmb375m for its 75% stake in the JV. Meanwhile, the company plans to issue Rmb1.8bn of corporate green bonds in the domestic market. The net proceeds would be used for the current capex plan, new acquisitions and refinancing of bank loans.

- **Canvest (1381.HK; Buy)** – Canvest announced a strategic cooperation agreement with (i) BOC & UTRUST Private Equity Fund Management; and (ii) Guangdong Finance Investment. UTRUST is a financial holding group under Guangdong local government. According to the agreement, the two parties will help Canvest to: (1) expand business and acquire new projects, as well as obtain new WTE projects in Guangdong Province; (2) coordinate relevant policy funds (e.g. PPP fund); and (3) establish a joint industrial fund for clean environment projects, which could support Canvest's technical upgrade and business development. In our view, this new arrangement could bring in more positives to Canvest: (1) With the support from the strategic partners, Canvest should be able to source more new WTE projects in Guangdong, thus strengthening its market position in the WTE industry of the region; and (2) The agreement should be viewed as a vote of confidence from Guangdong government, who seeks a quality partner with good track record in execution of environmental projects. We believe there could be more re-rating potential to Canvest if the company could monetize on the agreement, i.e. to have more new project wins or form the investment fund.

## Sector performance and outlook

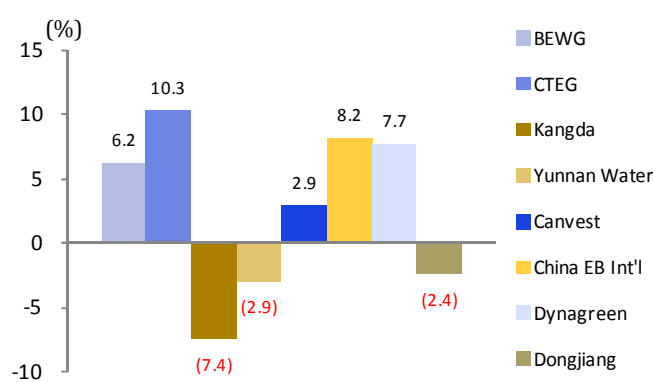
- Slight rebound in Jan:** The HK environmental sector advanced 3% MoM in Jan 2017, following the rebound of the general market. BEWG (371.HK; Buy), our top pick last month, surged 6.2% MoM. China Everbright (257.HK; NR) also surged 8.2% MoM, supported by the upbeat investment amount and overall planning of the 13<sup>th</sup> FYP on municipal waste treatment. Meanwhile, Beijing Origin Water (300070.CH; NR) declined 11.3% MoM as its FY16 earnings estimate announced by the company was slightly lower than expected.
- Suggest focusing on YNW and Canvest before results announcement:** Looking forward, the results season for FY16 will start soon. Within the HK environmental sector, we suggest that investors start paying attention to counters with potential high earnings growth in FY16. For instance, we estimate Canvest (1381.HK; Buy) to register 45% YoY net profit growth for FY16, mainly driven by construction revenue from new projects during 2H16. Yunnan Water (6839.HK; Buy) is another counter with high earnings growth in FY16. We estimate the counter to register 37% YoY growth in net profit, given the consistent contribution from both operational and construction revenues from new projects.

Figure 2: Performance of A-share listed co. in Jan 17



Source: Bloomberg, BOCOM Int'l

Figure 3: Performance of HK listed co. in Jan 17



Source: Bloomberg, BOCOM Int'l

Figure 4: Valuation summary

Company name	Stock ticker	Rating	TP	CP	Reporting Currency	EPS		EPS Consensus		P/E		P/B		Yield FY16E (%)
						FY16E	FY17E	FY16E	FY17E	FY16E (x)	FY17E (x)	FY16E (x)	FY17E (x)	
<b>HK shares</b>			(HK\$)	(HK\$)										
BEWG	371.HK	Buy	7.50	5.45	HKD	0.355	0.440	0.351	0.434	15.4	12.4	2.6	2.3	2.2
CTEG	1363.HK	Buy	2.05	1.71	RMB	0.110	0.130	0.111	0.135	13.7	11.6	2.6	2.2	1.3
Kangda	6136.HK	Neutral	1.85	1.88	RMB	0.159	0.212	0.168	0.220	10.4	7.8	1.0	0.9	1.2
YN Water	6839.HK	Buy	6.35	3.96	RMB	0.328	0.411	0.328	0.446	10.7	8.5	1.0	0.9	4.0
Canvest	1381.HK	Buy	4.85	3.86	HKD	0.198	0.270	0.188	0.251	19.5	14.3	2.8	2.4	0.8
China EB	257.HK	N/A	N/A	9.47	HKD	N/A	N/A	0.581	0.727	16.3	13.0	2.2	2.0	2.2
Dynagreen	1330.HK	N/A	N/A	3.60	RMB	N/A	N/A	0.302	0.396	10.5	8.0	1.2	1.1	1.4
Dongjiang	895.HK	N/A	N/A	13.18	RMB	N/A	N/A	0.540	0.634	21.5	18.3	3.2	2.3	0.7
<b>Average</b>										<b>14.8</b>	<b>11.7</b>	<b>2.1</b>	<b>1.8</b>	<b>1.7</b>
<b>A-shares</b>			(Rmb)	(Rmb)										
Chongqing Water	601158 CH	N/A	N/A	7.84	RMB	N/A	N/A	0.323	0.325	24.3	24.1	2.6	2.5	3.4
BJ Capital Co.	600008 CH	N/A	N/A	4.18	RMB	N/A	N/A	0.137	0.159	30.5	26.3	1.8	1.8	2.2
Grandblue Env.	600323 CH	N/A	N/A	14.59	RMB	N/A	N/A	0.698	0.852	20.9	17.1	2.3	2.1	1.0
BJ Origin Water	300070 CH	N/A	N/A	15.54	RMB	N/A	N/A	0.669	0.925	23.2	16.8	3.0	2.6	0.5
China Tianying	000035 CH	N/A	N/A	7.30	RMB	N/A	N/A	0.234	0.302	31.2	24.2	3.1	3.2	0.0
Wuxi Xuelang	300385 CH	N/A	N/A	37.71	RMB	N/A	N/A	0.731	1.004	51.6	37.6	5.1	2.6	0.3
Tus-Sound	000826 CH	N/A	N/A	34.11	RMB	N/A	N/A	1.312	1.639	26.0	20.8	4.0	5.1	0.5
Chengdu Xingrong	000598 CH	N/A	N/A	5.63	RMB	N/A	N/A	0.297	0.330	19.0	17.1	1.9	3.0	0.7
Dongjiang Env.	002672 CH	N/A	N/A	18.08	RMB	N/A	N/A	0.614	0.619	46.4	29.2	4.9	1.7	0.6
<b>Average</b>										<b>30.3</b>	<b>23.7</b>	<b>3.2</b>	<b>2.7</b>	<b>1.1</b>

Source: Bloomberg, BOCOM Int'l estimates for covered stocks

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**Company Rating**

Buy: Expect more than 20% upside in 12 months

LT Buy: Expect more than 20% upside but longer than 12 months

Neutral: Expect low volatility

Sell: Expect more than 20% downside in 12 months

**Sector Rating**

Outperform ("OP"): Expect more than 10% upside in 12 months

Market perform ("MP"): Expect low volatility

Underperform ("UP"): Expect more than 10% downside in 12 months

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