

I Hong Kong

ADD (no change)

Consensus ratings*: Buy 7 Hold 0 Sell 0

Current price:	HK\$7.94
Target price:	HK\$10.76
Previous target:	HK\$11.12
Up/downside:	35.6%
CGI / Consensus:	-3.5%
Reuters:	0855.HK
Bloomberg:	855 HK
Market cap:	US\$1,651m
	HK\$12,961m
Average daily turnover:	US\$1.87m
	HK\$14.69m
Current shares o/s:	1,623m
Free float:	48.1%

*Source: Bloomberg

Key changes in this note

- FY23F and FY24F revenue increased by 3.9% and 2.1%, respectively.
- FY23F and FY24 net profit decreased by 5.6% and 5.8%, respectively.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	1.1	-10	31.5
Relative (%)	-7.2	-13.4	54.9

Major shareholders	% held
Chairman, Mr Duan Chuan-lian	28.9
ORIX Corporation	17.8

Analyst

Mark Po

T (852) 3698 6318

E markpo@chinastock.com.hk

China Water Affairs

Lower-than-expected FY22 results; operations remain resilient

- China Water Affairs (CWA) reported its FY22 results, which were lower than we expected, given the lower-than-expected gross profit margin.
- Higher energy costs, a less favourable revenue mix, and spin-off-related expenses were the reasons for the lower-than-expected profitability.
- CWA separately disclosed its pipeline direct drinking water operations, which reported strong yoy growth in FY22. In our view, this will be one of its growth drivers.
- Despite its share price outperformance, CWA is trading at 5.9x FY23F P/E and 5.1x FY24F P/E, and with a yield of 4.3%, CWA's valuation still looks attractive. We reiterate our ADD rating, with a new target price of HK\$10.76 (down from HK\$11.12), based on 8x FY23F P/E, which is in line with its historical average.

FY22 results lower than we expected

CWA reported revenue of HK\$12,949.8m in FY22, up 25.2% yoy from HK\$10,345.5m in FY21. It reported a net profit of HK\$1,893.6m, representing a steady increase of 11.9% from HK\$1,692.5m in FY21. The Company's results were lower than we expected, given the higher-than-expected expenses. CWA declared a final dividend of HK\$0.18/share for FY22, up from HK\$0.16/share in FY21. The revenue contribution from water supply operation services and water supply connection income amounted to HK\$5,617.9m in FY22, up 18.7% yoy from HK\$4,733.5m in FY21. The revenue contribution from water supply construction services amounted to HK\$4,527.7m in FY22, up 22.8% yoy from HK\$3,685.8m in FY21. Revenue from city water supply operations and construction services amounted to HK\$10,347.1m in FY22, up 21.1% yoy from HK\$8,544.0m in FY21, representing approximately 79.9% of total revenue in FY22, down from 82.6% in FY21. The revenue contribution from sewage treatment and drainage operations services amounted to HK\$389.1m in FY22, up from 18.2% yoy from HK\$329.1m in FY21. The revenue contribution from sewage treatment and water environmental renovation construction services amounted to HK\$771.4m in FY22, up 3.3% yoy from HK\$747.1m in FY21. Revenue from the environmental protection segment amounted to HK\$1,250.8m in FY22, up slightly from HK\$1,205.2m in FY21. The environmental protection segment profit amounted to HK\$411.0m, up 39.8% yoy from HK\$294.0m in FY21. CWA separately disclosed its pipeline direct drinking water operations, which reported a 379.4% yoy increase in revenue in FY22. As at 31 Mar 22, CWA had developed over 2,000 direct drinking water projects (up from 1,200 at end of 1HFY22), serving 3m people.

Growth outlook

The direct drinking water industry has enormous room for growth and promising market prospects. The development of the pipeline direct drinking water business and the enhancement of service quality will become CWA's key development strategies in the next several years. CWA will continue to accelerate the development of its pipeline direct drinking water business in various regions to improve its service quality and provide urban and rural residents with better "last-meter" drinking water solutions. The Company will strive to fulfill the general desire of the people to improve their quality of life and take the lead to promote a healthy, low-carbon lifestyle. The General Office of the State Council issued "Opinions on Promoting Urbanisation with Counties and Towns as Vital Drivers", which provides opportunities for the Group's strategic implementation of urban-rural water supply integration and supply-drainage integration.

Financial Summary

	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Revenue (HK\$m)	10,346	12,950	14,447	16,089	18,147
Operating EBITDA (HK\$m)	4,096	4,694	5,422	6,174	6,941
Net Profit (HK\$m)	1,692	1,894	2,184	2,535	2,902
Core EPS (HK\$)	1.06	1.18	1.35	1.56	1.79
Core EPS Growth	15.9%	11.3%	13.9%	16.0%	14.5%
FD Core P/E (x)	7.47	6.71	5.89	5.08	4.43
DPS (HK\$)	0.31	0.34	0.39	0.45	0.52
Dividend Yield	3.90%	4.28%	4.92%	5.66%	6.51%
EV/EBITDA (x)	7.92	7.39	6.67	5.75	4.96
P/FCFE (x)	NA	4.44	4.26	2.38	1.91
Net Gearing	85.7%	77.3%	68.8%	53.1%	38.2%
P/BV (x)	1.20	0.99	0.89	0.79	0.70
ROE	17.8%	16.2%	15.9%	16.4%	16.6%
% Change In Core EPS Estimates			(5.54%)	(5.72%)	
CGI/consensus EPS (x)			0.96	0.99	

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

Forecast and TP adjustment

We raised our revenue forecasts for FY23F and FY24F by 3.9% and 2.1%, respectively, partly due to factoring in the revenue contribution from its direct drinking water operations. We cut our net profit forecasts for FY23F and FY24 by 5.6% and 5.8%, respectively, because of higher operating expenses. CWA is trading at 5.9x FY23F P/E and 5.1x FY24F P/E, and with a yield of 4.3%, its valuation still looks attractive. We reiterate our ADD rating, with a new target price of HK\$10.76 (down from HK\$11.12), based on 8x FY23F P/E, which is in line with its historical average.

Figure 1: Change in assumptions

Y/E March 31	FY23F			FY24F		
	Old	New	% change	Old	New	% change
Turnover (HKDm)						
City water supply operation and construction	10,603.5	11,508.6	9%	11,817.0	12,931.5	9%
Sewage treatment operation and construction	1,331.8	1,064.6	-20%	1,397.1	1,008.3	-28%
Property development and investment	444.2	494.5	11%	444.2	494.5	11%
Others	1,522.5	1,379.0	-9%	2,105.2	1,654.8	-21%
YoY Change (%)						
City water supply operation and construction	10.7	13.4		11.4	12.4	
Sewage treatment operation and construction	4.5	(8.3)		4.9	(5.3)	
Property development and investment	0	0		0	0	
Others	58.7	20.0		38.3	20.0	
Gross margin (%)						
			ppt			ppt
City water supply operation and construction	39.4	39.0	(0.4)	38.8	39.7	0.9
Sewage treatment operation and construction	42.7	42.2	(0.5)	42.7	43.2	0.5
Property development and investment	49.4	48.4	(1.0)	49.4	49.4	0
Concrete	18.0	18.0	0	18.0	18.0	0
Net margin (%)	13.3	13.3	0.0	13.3	13.3	0
			ppt			ppt
Net margin (%)	16.6	15.1	(1.5)	17.1	15.8	(1.3)
Cost (HKDm)						
S,G&A	(1,263.6)	(1,263.5)	(0.0)	(1,385.5)	(1,358.9)	(0.0)
Financial Expenses (HKD)	(482.2)	(537.3)	0.1	(546.7)	(598.9)	0.1
YoY Change (%)						
S,G&A	9.8	7.9		9.6	7.5	
Financial Expenses (HKD)	15.7	14.8		13.4	11.5	
Water tariff (HKD)						
Water tariff (HKD)	2.9	3.2	10.3%	3.0	3.4	12.0%
Volume (m3)						
Volume (m3)	1,400.4	1,329.2	-5.1%	1,610.5	1,528.5	-5.1%
YoY Change (%)						
Water tariff	5.0	10.0		5.0	5.0	
Volume	15.0	15.0		15.0	15.0	
Contribution from associates (HKDm)						
Contribution from associates (HKDm)	392.1	252.4	-35.6%	490.9	278.2	-43.3%
Net profit (HKDm)						
Net profit (HKDm)	2,314.7	2,184.2	-5.6%	2,691.1	2,535.0	-5.8%

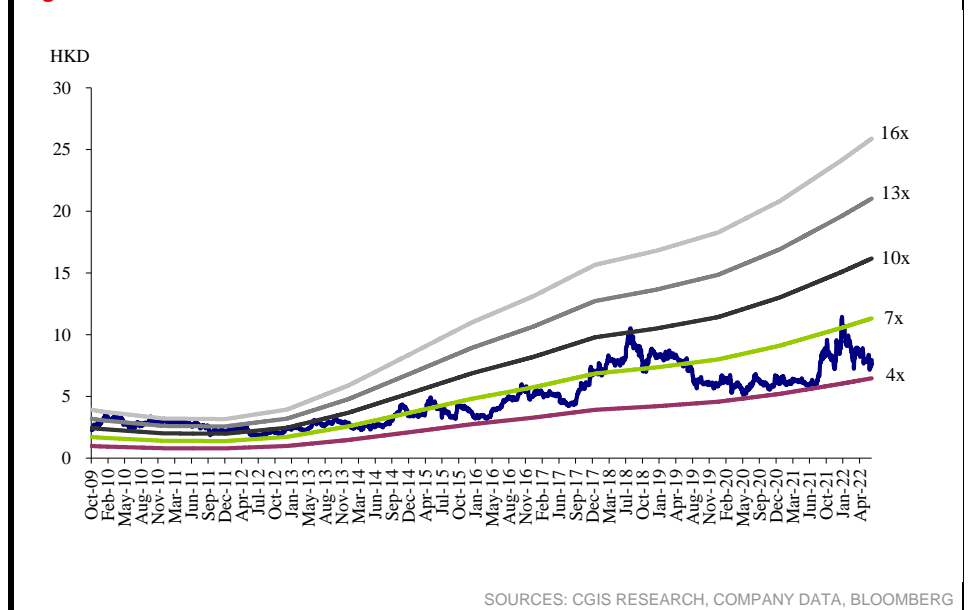
SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

Figure 2: Assumptions

	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Y/E March 31														
Turnover (HKDm)														
City water supply operation and construction	1,088.7	1,587.6	1,734.0	1,875.4	2,244.2	4,000.3	4,960.8	6,096.9	6,285.5	7,103.3	8,419.3	10,145.6	11,508.6	12,931.5
Sewage treatment operation and construction	48.6	46.4	50.9	82.4	169.9	339.0	552.9	786.9	1,405.6	948.0	1,076.3	1,160.5	1,064.6	1,008.3
Property development and investment	187.5	18.9	223.6	385.3	114.0	23.3	22.0	445.8	251.0	200.2	296.1	494.5	494.5	494.5
Others	153.3	244.0	242.2	403.5	330.5	377.3	172.1	250.7	360.1	446.8	553.8	1,149.2	1,379.0	1,654.8
YoY Change (%)														
City water supply operation and construction		45.8	9.2	8.2	19.7	78.2	24.0	22.9	3.1	13.0	18.5	20.5	13.4	12.4
Sewage treatment operation and construction		(4.5)	9.7	61.8	106.3	99.5	63.1	42.3	78.6	(32.6)	13.5	7.8	(8.3)	(5.3)
Property development and investment		(89.9)	1,080.8	72.3	(70.4)	(79.6)	(5.4)	1,923.3	(43.7)	(20.2)	47.9	67.0	0	0
Others		59.2	(0.8)	66.6	(18.1)	14.2	(54.4)	45.6	43.7	24.1	23.9	107.5	20.0	20.0
Gross margin (%)														
City water supply operation and construction	42.7	44.0	43.1	41.8	47.3	44.3	43.5	43.1	41.7	43.3	41.9	38.3	39.0	39.7
Sewage treatment operation and construction	41.3	46.1	46.1	46.1	50.9	45.9	43.4	44.8	42.5	44.8	43.7	41.2	42.2	43.2
Property development and investment	54.4	58.6	58.6	58.6	60.0	59.0	54.0	53.0	50.5	50.5	49.4	47.4	48.4	49.4
Concrete	48.0	174.9	50.0	50.0	50.0	50.0	50.0	18.0	18.0	18.0	18.0	18.0	18.0	18.0
Net margin (%)	13.5	12.3	12.3	12.3	14.3	14.3	14.3	13.3	13.3	13.3	13.3	13.3	13.3	13.3
Net margin (%)														
City water supply operation and construction	28.5	16.6	12.7	10.2	13.0	12.8	15.0	15.0	16.5	18.8	16.4	14.6	15.1	15.8
Cost (HKDm)														
S,G&A														
	(344.3)	(397.4)	(446.8)	(535.6)	(587.0)	(695.0)	(764.2)	(808.2)	(846.7)	(934.5)	(1,012.7)	(1,171.5)	(1,263.5)	(1,358.9)
Financial Expenses (HKD)														
	(102.7)	(86.8)	(86.5)	(106.9)	(117.4)	(170.8)	(251.2)	(289.1)	(319.2)	(429.2)	(370.6)	(468.1)	(537.3)	(598.9)
YoY Change (%)														
S,G&A														
		15.4	12.4	19.9	9.6	18.4	10.0	5.8	4.8	10.4	8.4	15.7	7.9	7.5
Financial Expenses (HKD)														
		(15.5)	(0.3)	23.6	9.8	45.5	47.0	15.1	10.4	34.5	(13.7)	26.3	14.8	11.5
Water tariff (HKD)														
	1.8	2.1	2.2	2.2	2.3	2.3	2.3	2.4	2.5	2.4	2.6	2.9	3.2	3.4
Volume (m3)														
	425.9	469.0	443.8	500.3	545.1	623.8	699.1	807.0	897.2	987.7	1,073.3	1,155.8	1,329.2	1,528.5
YoY Change (%)														
Water tariff														
		14.3	5.8	0.5	3.6	1.3	0	5.0	1.3	(1.4)	7.0	11.7	10.0	5.0
Volume														
		10.1	(5.4)	12.7	9.0	14.4	12.1	15.4	11.2	10.1	8.7	7.7	15.0	15.0

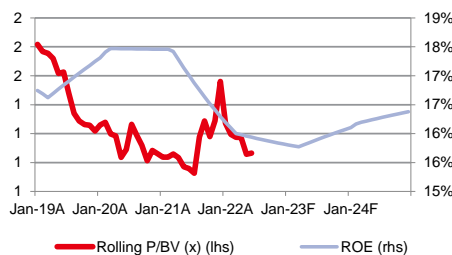
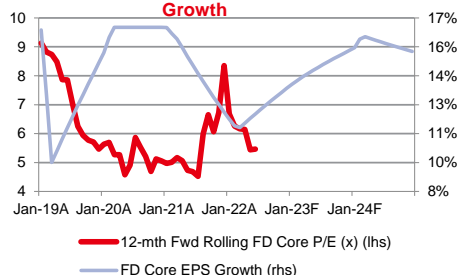
SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

Figure 3: CWA P/E band



SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

BY THE NUMBERS

P/BV vs ROE

12-mth Fwd FD Core P/E vs FD Core EPS Growth


Profit & Loss

(HK\$m)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Total Net Revenues	10,346	12,950	14,447	16,089	18,147
Gross Profit	5,109	5,866	6,686	7,533	8,420
Operating EBITDA	4,096	4,694	5,422	6,174	6,941
Depreciation And Amortisation	(770)	(903)	(1,053)	(1,153)	(1,253)
Operating EBIT	3,326	3,791	4,369	5,021	5,688
Financial Income/(Expense)	(211)	(345)	(366)	(332)	(282)
Pretax Income/(Loss) from Assoc.	213	235	258	284	313
Non-Operating Income/(Expense)	205	241	263	276	290
Profit Before Tax (pre-EI)	3,533	3,922	4,523	5,249	6,009
Exceptional Items	(3)	(6)	(6)	(6)	(6)
Pre-tax Profit	3,530	3,916	4,517	5,243	6,003
Taxation	(868)	(939)	(1,083)	(1,257)	(1,439)
Exceptional Income - post-tax					
Profit After Tax	2,662	2,977	3,434	3,986	4,563
Minority Interests	(970)	(1,084)	(1,250)	(1,451)	(1,661)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	1,692	1,894	2,184	2,535	2,902
Recurring Net Profit	1,695	1,898	2,189	2,540	2,907
Fully Diluted Recurring Net Profit	1,695	1,898	2,189	2,540	2,907

Cash Flow

(HK\$m)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
EBITDA	4,096	4,694	5,422	6,174	6,941
Cash Flow from Inv. & Assoc.					
Change In Working Capital					
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(845)	1,656	1,181	1,234	1,341
Net Interest (Paid)/Received	(371)	(468)	(537)	(599)	(671)
Tax Paid					
Cashflow From Operations	2,881	5,882	6,066	6,810	7,611
Capex	(4,000)	(4,000)	(4,500)	(3,000)	(3,000)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	(142)	(2,447)	(1,067)	(1,165)	(1,321)
Cash Flow From Investing	(4,142)	(6,447)	(5,567)	(4,165)	(4,321)
Debt Raised/(repaid)	388	3,435	2,527	2,773	3,475
Proceeds From Issue Of Shares	0	0	0	0	0
Shares Repurchased					
Dividends Paid	(494)	(513)	(591)	(680)	(781)
Preferred Dividends					
Other Financing Cashflow	(59)	(113)	(102)	(50)	27
Cash Flow From Financing	(166)	2,808	1,834	2,043	2,720
Total Cash Generated	(1,427)	2,243	2,334	4,689	6,009
Free Cashflow To Equity	(873)	2,870	3,026	5,418	6,764
Free Cashflow To Firm	(891)	(97)	1,037	3,244	3,961

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

BY THE NUMBERS... cont'd

Balance Sheet					
(HK\$m)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Total Cash And Equivalents	3,901	6,023	8,342	13,015	19,008
Total Debtors	2,951	3,946	4,402	4,903	5,530
Inventories	922	832	928	1,033	1,165
Total Other Current Assets	5,102	5,698	5,810	5,931	6,082
Total Current Assets	12,877	16,499	19,482	24,882	31,785
Fixed Assets	17,541	20,638	24,084	25,931	27,677
Total Investments	1,196	1,399	1,561	1,738	1,960
Intangible Assets	1,409	1,306	1,306	1,306	1,306
Total Other Non-Current Assets	14,015	17,223	17,373	17,528	17,703
Total Non-current Assets	34,161	40,566	44,324	46,503	48,646
Short-term Debt	5,262	7,692	8,581	9,557	10,779
Current Portion of Long-Term Debt					
Total Creditors	5,908	7,350	8,199	9,132	10,300
Other Current Liabilities	3,378	4,206	4,466	4,752	5,066
Total Current Liabilities	14,547	19,248	21,247	23,440	26,145
Total Long-term Debt	13,167	14,171	15,810	17,607	19,859
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	0	0	0	0	0
Total Non-current Liabilities	13,167	14,171	15,810	17,607	19,859
Total Provisions	2,374	3,162	3,423	3,706	4,013
Total Liabilities	30,088	36,582	40,479	44,753	50,017
Shareholders' Equity	10,513	12,969	14,563	16,418	18,539
Minority Interests	6,437	7,514	8,763	10,214	11,875
Total Equity	16,950	20,483	23,326	26,632	30,414

Key Ratios					
	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Revenue Growth	18.9%	25.2%	11.6%	11.4%	12.8%
Operating EBITDA Growth	18.2%	14.6%	15.5%	13.9%	12.4%
Operating EBITDA Margin	39.6%	36.2%	37.5%	38.4%	38.2%
Net Cash Per Share (HK\$)	(9.17)	(9.76)	(9.89)	(8.72)	(7.17)
BVPS (HK\$)	6.63	7.99	8.97	10.11	11.42
Gross Interest Cover	8.98	8.10	8.13	8.38	8.47
Effective Tax Rate	24.6%	24.0%	24.0%	24.0%	24.0%
Net Dividend Payout Ratio	29.0%	29.1%	29.0%	28.7%	28.9%
Accounts Receivables Days	103.6	97.2	105.5	105.8	104.9
Inventory Days	54.11	45.18	41.37	41.94	41.25
Accounts Payables Days	400.7	341.5	365.6	370.7	364.5
ROIC (%)	12.3%	11.6%	11.5%	12.2%	13.3%
ROCE (%)	10.4%	10.1%	10.1%	10.4%	10.6%
Return On Average Assets	6.47%	6.39%	6.30%	6.40%	6.39%

Key Drivers					
	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Water Tariff (HKD)	2.6	2.9	3.2	3.4	3.5
Volume (k tonnes)	1,073.3	1,155.8	1,329.2	1,528.5	1,757.8

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

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Distribution of stock ratings and investment banking clients for quarter ended on 31 Mar 2022		
632 companies under coverage for quarter ended on 31 Mar 2022		
	Rating Distribution (%)	Investment Banking clients (%)
Add	70.3%	0.8%
Hold	22.0%	0.0%
Reduce	7.8%	0.2%

Spitzer Chart for stock being researched (2 year data)

China Water Affairs (855 HK)

RECOMMENDATION FRAMEWORK

Stock Ratings Definition:

Add	The stock's total return is expected to reach 15% or higher over the next 12 months.
Hold	The stock's total return is expected to be between negative 10% and positive 15% over the next 12 months.
Reduce	The stock's total return is expected to fall below negative 10% over the next 12 months.

The total expected return of a stock is defined as the sum of the:(i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings Definition:

Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

Country Ratings Definition:

Overweight	An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.

Analyst Certification

The analyst who is primarily responsible for the content of this report, in whole or in part, certifies that with respect to the securities or issuer covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject, securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by the analyst in this report.

Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the securities covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the securities covered in this research report three business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong-listed companies covered in this report; and (4) have any financial interests in the Hong Kong-listed companies covered in this report.

#11