China

China Strategy

More SOE privatization to come?

- We have seen more SOE privatization cases in the past 12 months though not all were delisted successfully.
- Some SOEs have been trading deeply below book value for a long time, so their listings have lost the fundraising function.
- We are more likely to see a proposed privatization if the listing vehicle is not very important strategically and if the controlling shareholder owns more than 50%.
- We believe investors should pay attention to Huadian Fuxin, Beijing Jingneng, Datang Renewable, COSCO Shipping International, APT Satellite, Tianjin Development and CRCC High-Tech.

SOE privatization becoming more common

In the past, SOE (H-shares and red chips) privatization was not very common, as many parent companies considered a listing vehicle to be a valuable resource. However, the situation has changed gradually, as there have been at least three proposed privatizations in the past 12 months: Harbin Electric (1133.HK), AsiaSat (1135.HK) and Huaneng Renewables (0958.HK), which was announced in early September.

Some listings no longer have a fundraising function

Although a listing vehicle can be a valuable resource, more parent companies have become willing to consider a privatization because the listing vehicle is nearly useless if the stock has traded far below book value for a long time. The top authorities have an implicit requirement that prevents SOEs from issuing new shares below book value.

Factors affecting privatization

In the case of Harbin Electric, AsiaSat and Huaneng Renewables, the controlling shareholder owns more than 50%, so the cost of privatization will be lower. The importance of the listing vehicle also plays a key role. For example, CITIC Group and Huaneng Group would still have other listing vehicles after the privatization of AsiaSat and Huaneng Renewables. This makes it much easier to make a privatization decision. Harbin Electric is one of the smallest central SOEs (market cap: HK$3.5bn), which implies that it is not very important to keep the listing status from the perspective of the SASAC.

Screening criteria

We screened a list of SOEs to see which companies deserve more attention from the privatization angle: (i) P/Bv below 0.5x; (ii) the controlling shareholder owning more than 50%; and (iii) the listing vehicle being not very important strategically, based on the discussion above. We also removed stocks with a market cap below HK$2bn (too small for institutional investors) or above HK$30bn (the cost of privatization may be too big). After the screening exercise, we believe the following stocks may deserve more attention: Huadian Fuxin (0816.HK), Beijing Jingneng (0579.HK), Datang Renewable (1798.HK), COSCO Shipping International (0517.HK), APT Satellite (1045.HK), Tianjin Development (0882.HK), and CRCC High-Tech (1786.HK).

Huadian Fuxin

Huaneng Renewables is the new energy business arm of Huaneng Group. Similarly, Huadian Fuxin is the new energy business arm of Huadian Group, focusing on various kinds of renewable and clean energy. The parent company holds a 62.76% stake in Huadian Fuxin. It is trading at 4.2x 2019F P/E, based on market consensus, and 0.48x P/Bv.

Datang Renewable

The Company is the clean energy business arm of Datang Group, focusing on wind power. The parent company owns a 65.6% stake. It is trading at 3.8x 2019F P/E, based on consensus estimates, and 0.46x P/Bv. *(more on next page)*

Figure 1: Valuation table

Ticker	Company name	Price (HK$)	Market cap (HK$m)	P/E (x)	2019F P/E (x)	2020F P/E (x)	P/Bv (x)	Dividend yield (%)	3-month average daily turnover (HK$m)
816 HK Equity	Huadian Fuxin Energy Corp Ltd	1.38	11,603	4.63	4.21	3.61	0.48	4.67	6,024,458
579 HK Equity	Beijing Jingneng Clean Energy Co Ltd	1.32	10,883	4.41	4.61	4.14	0.47	5.74	1,618,960
1798 HK Equity	China Datang Corp Renewable Power Co Ltd	0.76	5,528	4.62	3.79	3.32	0.46	2.98	959,280
517 HK Equity	COSCO SHIPPING International Hong Kong Co Ltd	2.27	3,480	12.16	n.a.	n.a.	0.44	7.05	938,021
1045 HK Equity	APT Satellite Holdings Ltd	2.72	2,532	4.99	n.a.	n.a.	0.45	5.88	884,911
882 HK Equity	Tianjin Development Holdings Ltd	2.14	2,296	5.92	n.a.	n.a.	0.20	3.76	996,124
1786 HK Equity	CRCC High-Tech Equipment Corp Ltd	1.38	2,097	11.53	9.64	7.99	0.35	4.11	720,632

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

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Beijing Jingneng

Beijing Jingneng is a local SOE, controlled by the Beijing municipal government (71.4% stake). As with Huadian Fuxin and Datang Renewable, the Company is a clear energy utilities operator. The latest P/Bv of the Company is 0.47x, with a 2019F P/E of 4.6x.

COSCO Shipping International

COSCO Shipping International provides shipping-related services. It offers shipping, logistics, shipbuilding and ship repair services, ship trading agency services, marine insurance brokerage services, marine equipment and spare parts, coating products, marine fuel and other shipping-related products. The parent company controls a 66.1% stake. The Company has kept a low profile for a long time and has a net cash position of more than HK$6bn, equivalent to 1.7x of its market cap.

APT Satellite

China SatCom owns a 53.23% stake of APT Satellite. There are only two licensed satellite operators in China: a) China SatCom and b) Asia Sat. The latter has just completed the privatization at a P/Bv of 1.1x. Since China SatCom (601698.CH) was listed on the Shanghai Stock Exchange this year and is trading at 5.74x 2019F P/Bv, this makes the listing status of APT Satellite less important. In particular, it has lost most of the fundraising function at 0.45x P/Bv.

Tianjin Development

Like COSCO Shipping International, Tianjin Development has remained very low profile for a long time, with a net cash position of more than HK$4.5bn, equivalent to nearly 2x its market cap. The parent company, Tianjin Pharmaceuticals, owns a 62.8% stake in the conglomerate.

CRCC High-Tech

CRCC High-Tech is a railway maintenance machinery manufacturer. It provides machinery and parts sales, and overhaul and maintenance services. CRCC (1186.HK) owns a 65% stake in the Company. It was listed on the main board in December 2015 at HK$5.25 per share, and the latest price is HK$1.38 (0.35x P/Bv).

Figure 2: Recent cases of SOE privatization

Ticker	Company name	Offer price (HK$)	Implied P/Bv (x)	Closing price before the announcement (HK$)	Date of announcement	Remarks
1133 HK Equity	Harbin Electric	4.56	0.44	2.5	24-Dec-18	The privatization failed marginally.
1135 HK Equity	AsiaSat	10.22	1.1	8.28	24-Jun-19	Successfully delisted.
958 HK Equity	Huaneng Renewables	TBC	TBC	n.a.	n.a.	Expressed the intention of privatization on 2 Sep 2019.

SOURCES: CGIS RESEARCH, COMPANY DATA

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We are transferring the rating mechanism from "BUY, SELL, HOLD" to "ADD, REDUCE, HOLD". Please refer to the definitions below.

Explanation on Equity Ratings (Existing mechanism (will be replaced by new mechanism by 01/09/19))

BUY : share price will increase by >20% within 12 months in absolute terms

SELL : share price will decrease by >20% within 12 months in absolute terms

HOLD : no clear catalyst, and downgraded from BUY pending clearer signal to reinstate BUY or further downgrade to outright SELL

Explanation on Equity Ratings (New mechanism)

ADD : The stock's total return is expected to exceed 10% over the next 12 months.

REDUCE : The stock's total return is expected to fall below 0% or more over the next 12 months.

HOLD : The stock's total return is expected to be between 0% and positive 10% over the next 12 months.

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