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Corporate: Surging on hydropower

By Francis Tan

Asia Power's acquisition of plants in China boosts earnings and investor appeal

The once-sleepy **Asia Power** Corp Ltd has emerged as one of the top three performers this year on the Singapore Exchange — behind Xpress Holdings and LKN-Primefield — with a 127% surge in share price to 29 cents last Thursday. In early January, as interest in China stocks was mounting, the company announced that it had won the rights to develop two hydropower electricity-generating plants in Sichuan province, China. And, following the release of its full-year results in March, the company went on a roadshow to spread the word of its “relentless pursuit to focus on renewable energy power generation plants as its main engine of growth”.

Asia Power currently operates seven power plants in Heilongjiang, Jiangsu and Sichuan provinces, selling the electricity it generates to the government's power grid. The combined installed capacity of these plants is 509mw, but the company only has associate stakes in half of the capacity. Three of the seven plants are hydropower plants, accounting for a quarter of the installed capacity. Last year, the three hydropower plants contributed a quarter of **Asia Power**'s net profit, or \$2.5 million. But that should increase this year as a result of full-year contributions from two of the plants — one only began turning in profits in March last year, while the other, from September.

And, looking further ahead, the rights it has secured to develop two more plants in Sichuan should grow its profits further. Construction of the first plant, which will have a capacity of 40mw, is slated to kick off in November in Huzhu. Costing about 200 million renminbi (\$1 approx five renminbi), it is due to begin generating electricity by the end of next year. According to **Asia Power**'s chief financial officer Tan Khoon Guan, the

second power plant at Xisujiao is scheduled to be completed by early 2008. However, details of this plant are still being finalised.

The company is also tightening its grip on some of its power plants. Just last week, **Asia Power** raised its stake in the Chongqing hydropower plant to 31.6% from 25.9%, with a total cumulative cost of about US\$6 million (\$1 approx US\$0.62). The plant has been in operation since November 2004. The group also increased its stake in the Anning River hydropower plant from 30% to 35% in December. In financial year 2005, Chongqing contributed \$332,000 in pre-tax profits while Anning River, which started operations in March, contributed \$1.3 million. **Asia Power**'s entire stake in Anning River cost 20.7 million renminbi.

Asia Power received \$3.9 million in dividends from associates last year, more than twice the \$1.85 million it collected in 2004. And, the company expects to see even higher payouts this year. Its dominant position in the associates helps to safeguard its investments. "In every investment or acquisition that we enter into, our strategy is always to be the largest shareholder in the company," says Tan.

Tariff hikes kick in

As for **Asia Power**'s subsidiaries, almost all of the 15% increase, or \$12.7 million, in turnover last year came from its largest power plant, the coal-fired 225mw Heilongjiang plant. Most of the gain arose from the 15% to 20% hikes in electricity tariffs implemented last August and September. Steam tariffs were similarly raised by 15% to 20% on a staggered basis in the last quarter. Supply of steam accounted for about a third of sales at the Heilongjiang plant.

Those tariff hikes helped mitigate the rise in fuel prices. Although the price of coal doubled last year, **Asia Power**'s gross margins only slipped slightly to 12.2% from 14.1% the previous year. Besides the higher tariffs, Tan also explains that **Asia Power**'s Heilongjiang plant uses "low heating" coal from Inner Mongolia, which tends to deteriorate in quality if transported over long distances and so doesn't command a very high price. Prices of this low-grade coal climbed less than 20% last year, Tan says.

The rapid build-up of the company's power generation assets has driven a steep rise in its earnings. Last year, **Asia Power**'s net profit surged almost 90% to \$10.1 million, with most of the gain coming from its associates, whose aggregate contribution doubled to \$8.5 million. In addition, 35%-owned Shenzhen Nari Technologies, which designs, manufactures and sells power automation systems for more than 400 power stations in China, contributed about \$2.5 million of the increased profits.

Asia Power's shares have risen sharply in the past year without any valuation guidance from analysts. But their valuations don't seem stretched. At their current level, they are priced at 10.6 times 2005 earnings and 1.7 times net tangible assets. With **Asia Power**'s management on the lookout for more power-generation assets, and demand for electricity in China growing fast, its shares are unlikely to run out of steam soon.