

# Chiho Environmental (976 HK)

## Business recovery ongoing; in good timing to chase for new growth

Chiho Environmental Group (CEG) is one of the largest metal recyclers in the world. The Company has major business presence in Asia, Europe and North America. We discussed Chiho's business recovery path with mgmt. recently. We think the Company is on track to a recovery of existing business, and is fostering new growth in China through a JV with China Hongqiao (1378 HK, BUY). Trading at only 0.33x PBR, CEG deserves a re-rating for potential fundamental improvement, in our view. We suggest investors put the name on the radar.

- Global leader in metal recycling.** In 2016, CEG acquired Scholz Holding GmbH (Scholz), a Germany-based company which had accumulated recycling know-how over 150 years. Since then, CEG has become one of the largest global scrap metal recycling companies with extensive operations in the recycling of ferrous and non-ferrous metal scraps, end-of-life cycle vehicles, electronic scraps and the production of secondary aluminum ingots from aluminum scraps. By end-2020, the Company has more than 200 processing plants and yard operations in Asia, Europe and America.
- Business back on track.** CEG experienced earnings volatility in 2019-20 mainly due to 1) scrap material import policy adjustment by Chinese government; and 2) economic and lockdown impacts caused by COVID-19. In 2020, the board of CEG replaced the management team, and the team carried out business restructuring by 1) shifting import-based Chinese business units to SE Asia countries such as Malaysia, India and Thailand; and 2) divesting Southwest operations in the US to improve business efficiency. CEG reported a turnaround in profit after tax from a loss of HK\$33.5mn in 1Q20 to a gain of HK\$57.0mn in 1Q21. We believe CEG's metal recycling business is back on track.
- Chasing for new growth in China.** We think China's net-zero development strategy will boost metal recycling business and create good opportunities for CEG to foster new growth. CEG's wholly owned subsidiary, Scholz, had formed a JV with China Hongqiao in Shandong China for 100k units of end-of-life vehicle (ELV) recycling and 500k tonnes of secondary aluminum production per annum. The JV had kicked off construction in Feb 2021. CEG planned to product the first can of aluminum liquid by end-2021, and ramp up phase 1 capacity (50k ELV/200k secondary aluminum) in 2022.
- Time for a re-rating.** We think there are two major catalysts for CEG. On one hand, CEG's existing metal recycling business is resuming profitability with strong earnings rebound outlook on the back of good commodity pricing. On the other hand, we think the progress of Shandong JV will strengthen market expectation for future earnings growth. YTD, CEG's share price has exhibited significant rebound. However, trading at only 0.33x PBR, CEG still has room for further re-rating, in our view.
- Risks:** Controlling shareholder's debt repayment pressures; insufficient trading liquidity.

### Earnings Summary

(YE 31 Dec)	FY16A	FY17A	FY18A	FY19A	FY20A
Revenue (HK\$ mn)	3,211	18,491	20,913	15,363	13,368
YoY growth (%)	n/a	475.8	13.1	(26.5)	(13.0)
Net profit (HK\$ mn)	(440)	427	401	(129)	(848)
EPS (HK\$)	(0.27)	0.27	0.25	(0.08)	(0.53)
YoY growth (%)	n/a	n/a	(0)	n/a	n/a
Consensus EPS (HK\$)	n/a	n/a	n/a	n/a	n/a
P/E (x)	n/a	3.4	3.6	n/a	n/a
P/B (x)	0.36	0.29	0.28	0.30	0.33
Yield (%)	nil	nil	nil	nil	nil
ROE (%)	-10.7	8.4	7.8	-2.6	-18.9
Net gearing	81.6	62.7	59.7	40.7	30.9

Source: Company data, Bloomberg, CMBIS

**NOT RATED**

Current Price

HK\$0.91

### Environmental

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#### Stock Data

Mkt Cap (HK\$ mn)	1,461
Avg 3 mths t/o (HK\$ mn)	3.0
52w High/Low (HK\$)	1.08/0.18
Total Issued Shares (mn)	1,605

Source: Bloomberg

#### Shareholding Structure

Tu Jianhua	60.95%
Zhang Mingjie	8.94%
Free float	30.11%

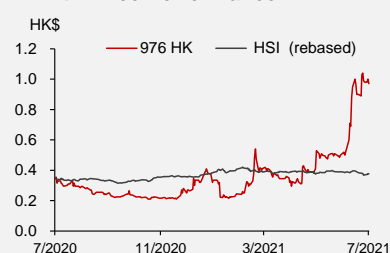
Source: HKEx

#### Share Performance

	Absolute	Relative
1-mth	94.0%	101.4%
3-mth	193.9%	205.7%
6-mth	189.6%	196.9%

Source: Bloomberg

#### 12-mth Price Performance



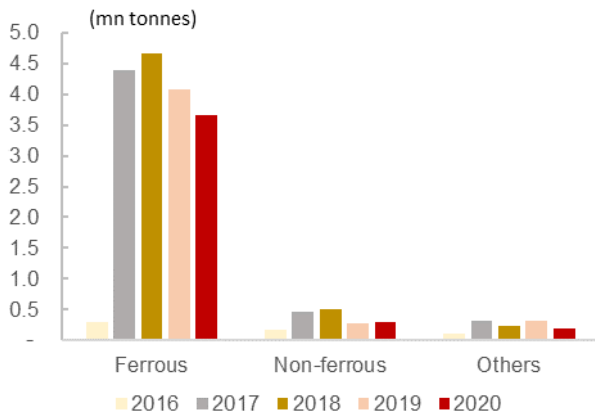
Source: Bloomberg

#### Auditor: PwC

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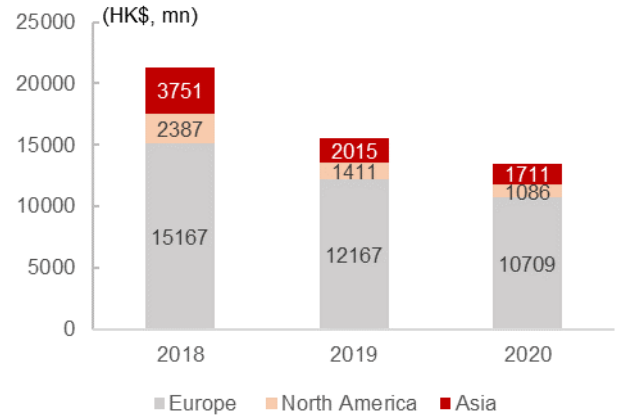
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**Figure 1: CEG's recycled material sales record**



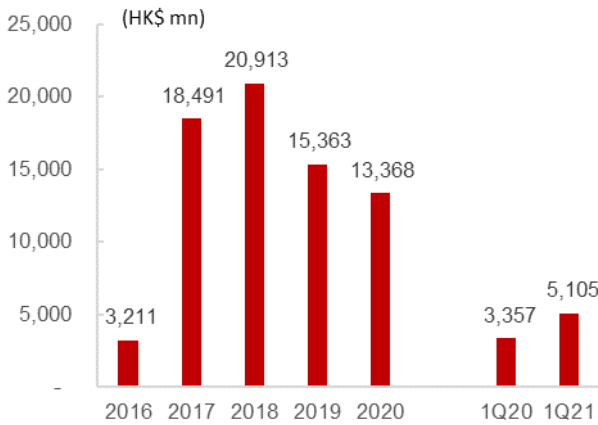
Source: Company data, CMBIS

**Figure 2: Geographical distribution of revenue in 2018-20**



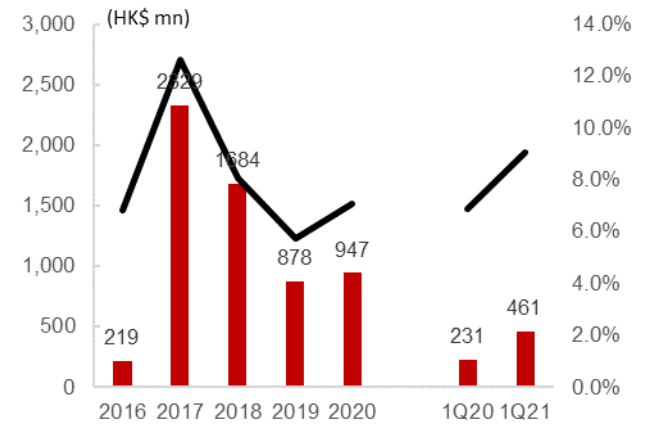
Source: Company data, CMBIS

**Figure 3: CEG's revenue trend**



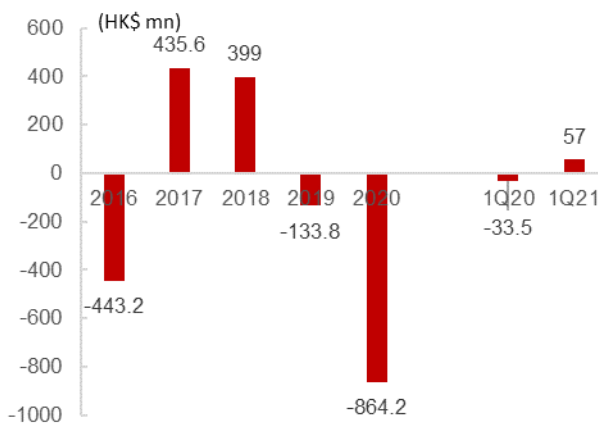
Source: Company data, CMBIS

**Figure 4: CEG's GP vs. GPM**



Source: Company data, CMBIS

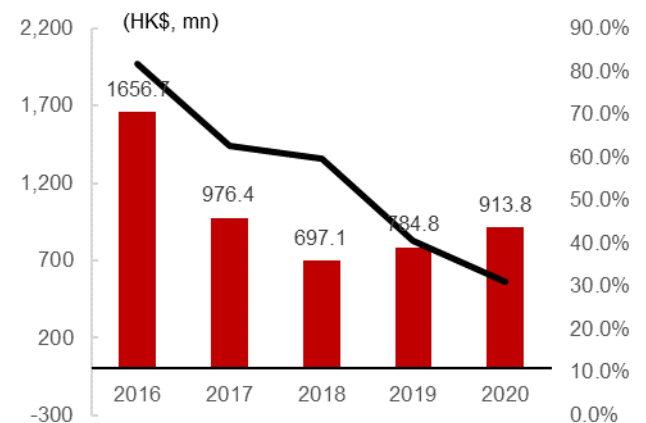
**Figure 5: CEG's profit after tax trend**



Source: Company data, CMBIS

Note CEG made asset provision of HK\$519.2mn in 2020

**Figure 6: CEG's cash level movement and net gearing trend**



Source: Company data, Bloomberg, CMBIS estimates

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