

# Long: CK Hutchison Holdings

Ticker: CKHUY

Enterprise Value: \$67.5B

Market Cap: \$48.3B

Stock Price: \$12.53

Target Price: \$16.62

Expected Return: 32%

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Written by: Mike Gorlon

# Business Overview

- Multinational conglomerate with 5 core businesses in ports, retail, infrastructure, energy, and telecommunications
- Headquartered in Hong Kong
- Founded in 1950 by Li Ka-shing
- Separated operating assets and real estate assets in 2015
- Merged Cheung Kong Holdings with Hutchison Whampoa in 2015 to form CK Hutchison

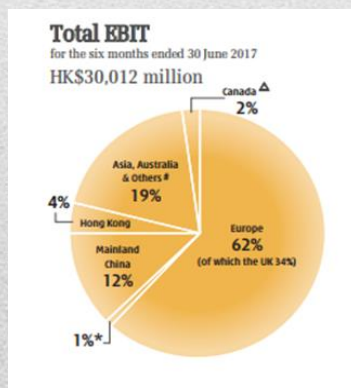
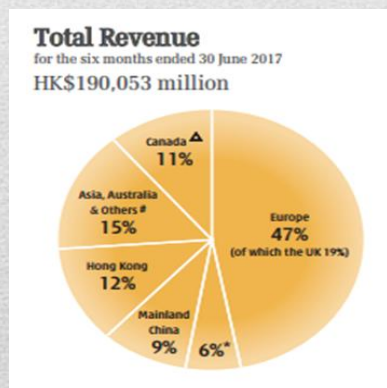
# Ownership Structure

## *CK Hutchison Holdings Ownership Structure*

<i>CK Hutchison Holdings Ownership Structure</i>							
CK Hutchison Holdings							
Hutchison Telecommunications Hong Kong Holdings (66.09%)	Hutchison Telecommunications (Australia) (87.87%)	CK Infrastructure Holdings (75.67%)	Hutchison China MediTech (60.36%)	Husky Energy (40.18%)	Hutchison Port Holdings (30.07%)	TOM Group (36.73%)	CK Life Sciences Int'l. (45.32%)
		Power Assets Holdings Limited (38.87%)					
		HK Electric Investments (33.37%)					

# Breakdown by EBIT, Revenue and Country

- Majority of revenue (47%) comes from Europe of which 19% is the UK
- 62% of EBIT comes from Europe of which 34% is from the UK
- Retail makes up the largest portion of revenue at 39%



	Unaudited Results for the six months ended 30 June 2017 HK\$ millions	
	HK\$ millions	%
<b>Revenue <sup>(1)</sup></b>		
Ports and Related Services <sup>(1)</sup>	16,195	8%
Retail	73,557	39%
Infrastructure	25,918	14%
Husky Energy	21,184	11%
3 Group Europe	33,215	17%
Hutchison Telecommunications Hong Kong Holdings	5,069	3%
Hutchison Asia Telecommunications	3,829	2%
Finance & Investments and Others	11,086	6%
<b>Total Revenue</b>	<b>190,053</b>	<b>100%</b>

Sources: Interim Report ending June 30, 2017

# Ports and Related Services

- Has 51 ports spanning across 26 countries throughout Asia, the Middle East, Africa, Europe, the Americas and Australasia
- Including cruise ship terminals, airport operations, distribution centers, rail services, and ship repair facilities
- According to CK's website, they handled a combined throughput of 81.4 million Twenty-Foot Equivalent Unit (TEU) of cargo capacity
- 8% of total revenue and 12% of total EBIT as of June 30, 2017



# Retail

- Owns A.S. Watson Group which is the largest health and beauty retailer in Asia and Europe
- Has over 13,700 retail stores in 21 countries worldwide
- Retail segment has health & beauty, perfumes and cosmetics, food, electronics, wine, and beverages
- Operates retail chains such as Kruidvat, Superdrug, Rossmann, Savers, Trekpleister, Drogas and Spektr
- Makes up the largest percentage of total revenue



# Infrastructure

- Holds a 75.67% interest in CK Infrastructure Holdings (stock code: 1038)
- Has investments in infrastructure for energy, transportation, water, waste management, energy-from-waste and energy management services
- Operates mainly in the UK, Australia, New Zealand, Canada, the U.S., Continental Europe, United Arab Emirates, Hong Kong and Mainland China
- Has direct investments in Australian Gas Networks, Dutch Enviro Energy Holdings, Northumbrian Water Group and Park’N Fly
- CK Infrastructure has a good balance sheet with total liabilities of \$5B (HKD:USD of .13) and total equity of \$12.8B.
- Free cash flow has been positive for 8 years straight with the last negative free cash flow being in 2008

	<i>TTM</i>	<i>2016</i>	<i>2015</i>	<i>2014</i>	<i>2013</i>	<i>2012</i>
<b>Operating Margin</b>	38%	36%	58%	34%	20%	36%
<b>Return on Equity</b>	10%	9%	11%	39%	17%	15%
<b>Return on Invested Capital</b>	9%	8%	10%	33%	15%	15%
<b>Free Cash Flow (USD,Mil)</b>	416.39	508.17	488.54	335.4	303.68	160.16



Source: Morningstar

# Energy

- Has a 40.18% interest in Husky Energy Inc.
- Husky Energy operates in Western and Atlantic Canada, the U.S. and the Asia Pacific region with Upstream and downstream business segments
- Good balance sheet with Debt to Equity ratio of 31% and CAD 2.4B in cash and CAD 200M in short term debt
- Generated 1 Billion in Free Cash Flow over the past 12 months

	TTM	2016	2015	2014	2013	2012
Free Cash Flow (CAD)	1.106B	266M	755M	562M	(383M)	488M





# Telecommunications

- Serves 130 million active customers across the world
- Holds a majority interest in Hutchison Telecommunications Hong Kong Holdings (Ticker Symbol: HTHKH)
- Operates 3 branded mobile networks in Austria, Italy, Ireland, Sweden and the U.K.
- Has a joint venture with Vodafone Group to provide service in Australia
- Operates mobile networks in Indonesia, Sri Lanka and Vietnam

# Finance & Investments

- *Hutchison Whampoa* - Conglomerate that dates back to 1863 with revenue of \$50B and over 200,000 employees
- *Hutchison China MediTech Limited* – Major drug manufacturer
- *CK Life Sciences Int'l* – Provides research and development, manufacturing, commercialization, marketing and selling of health and agricultural products
- *TOM Group Limited* – Operates in 5 segments: Mobile Internet Group, E-Commerce Group, Publishing Group, Social Network Group, and Advertising Group
- *Hutchison Water* – Develops technology for identifying and counting microorganisms in water

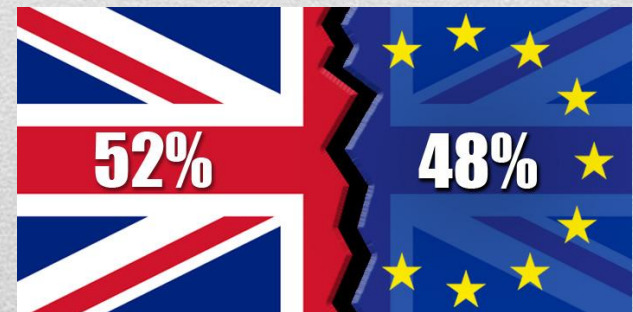
# Chairman



- Li Ka-shing was born in 1928
- He was forced to quit school when he was 12
- Started Cheung Kong Industries in the 1950's and developed it into the world conglomerate it is today
- Compounded capital at a comparable rate to Warren Buffett
- Selected as one of the world's best CEOs by Barron's
- Owns 30% of shares as of June 30, 2017 which aligns him with other shareholders
- His son, Victor Li Tzar-kuoi, owns another 28% as of June 30, 2017 and is the Co-Managing Director and Deputy Chairman

# Why Is It Undervalued?

- Conglomerates usually sell at a discount
- Brexit
- Foreign exchange and foreign translation impact on holding company's financials





# Relative Valuation to Selected Peers

Company	Market Cap (USD)	Net Income (USD)	P/S	P/B	P/E	Interest Coverage	Debt/Equity
<b>CK Hutchison</b>	<b>48.3B</b>	<b>4.4B</b>	<b>1.5</b>	<b>0.9</b>	<b>11.1</b>	<b>5.9</b>	<b>0.7</b>
Jardine Strategic Holdings	47.7B	3.8B	0.8	1.7	12.6	32.8	0.2
Softbank	95.8B	6.87B	1.2	2.3	14.5	2.5	2.5
Ichan Enterprises	9B	1.9B	0.4	1.9	4.5	-1.5	2.3
Berkshire Hathaway	454.3B	18.67B	1.9	1.5	24.2	10.6	0.3
General Electric	157.1B	7.5B	1.3	2.1	21.2	2.8	1.4
Mitsubishi	39.6B	4.63B	0.6	0.8	8.6	10.3	0.8
Average of each company	121.69B	6.82B	1.10	1.60	13.81	9.06	1.17

Source: Morningstar

- Undervalued to selected peers based on price to book, overvalued based on price to sales, and trades in line based on price to earnings

# Valuation

- Possible upside of 17.5% if share price (USD) closes the discount with book value and Price to Book approaches 1.0

Market Cap (USD) **48.3B**

Market Cap (HKD) **378.245B**

Book Value (USD) **56.8B**

Book Value (HKD) **436.941B**

- Possible upside of 19% (base case) if P/E multiple reaches 13

Current Share Price: \$12.53

Current Earnings per share: \$1.15

Current P/E: 11

Expected P/E: 13

Expected Price: \$14.95

- Possible upside of 37% (bull case) if P/E multiple reaches 15

Current Share Price: \$12.53

Current Earnings per share: \$1.15

Current P/E: 11

Expected P/E: 15

Expected Price: \$17.25

- Other possible upside case would be if the company manages Brexit well and earnings improve upwards. If P/E is at 10 and EPS are \$1.50 then there would be close to 20% upside

# Sum-of-the-Parts Valuation

		% of total EBIT	TTM EBIT (HKD)	Exchange Rate to USD	EBIT in USD	Multiple	Value	Notes
1	Ports and Related Services	12%	7,468.00	0.13	970.84	12	11,650.08	
2	Retail	17%	11,953.00	0.13	1,553.89	12	18,646.68	
3	Infrastructure	40%	21,820.00	0.13	2,836.60	10	28,366.00	
4	Husky	3%	3,656.00	0.13	475.28	N/A	4,760.00	(Market cap of \$11.9B times 40.18% ownership)
5	3 Group Europe	25%	14,938.00	0.13	1,941.94	10	19,419.40	
	Hutchison Telecommunications Hong Kong Holdings	2%	996.00	0.13	129.48	N/A	1,123.53	(Market Cap of 1.7B times 66.09% ownership)
	Hutchison Asia Telecommunications	0%	1,050.00	0.13	136.50	10	1,365.00	
	Vodafone Hutchison Australia	0%	Not Reported	0.13	N/A	N/A	441.00	(Market cap of \$882M times 50% ownership)
6	Finance & Investments	1%	1,076.00	0.13	139.88	10	1,398.80	
		<b>Total (HKD)</b>	<b>62,957.00</b>	<b>Total (USD)</b>	<b>8,184.41</b>		<b>87,170.49</b>	
						Cash	19,810.70	
						Debt	42,867.63	
						Net Debt	(23,056.93)	
						Value	64,113.56	
						Shares Outstanding (millions)	3,857	
						Value per share	16.62	

\*EBIT only includes CK Hutchison's portion



# Catalysts

- Possible share repurchase
- Possible spin off of assets can unlock value
- Separation of holding company and real estate properties perform and unlock value
- Market realizes that the equity is undervalued based on a sum-of-the-parts valuation

# Risks

- Foreign exchange rate risk due to business operations in multiple countries
- Brexit
- Possible key man risk since Li Ka-shing is 92 and is transitioning his son to take over leaves uncertainty with investors