

# Inovance Technology (300124.CH)

## New Energy and Railway Transportation Business Helping to Drive the Second Take-off of the Company

19 July 2017

China | Automobile Components | Company Initiation

### Company profile: Excellent Leader in the Field of Industrial Control Automation

Shenzhen Inovance Technology Co., Ltd., was established in 2003 and listed on the GEM of Shenzhen Stock Exchange in 2010. Inovance Technology is a medium- and high-end equipment manufacturer focusing on the industrial automation control products. The total number of employees is 4,522. The products are widely used and the business scope covers:

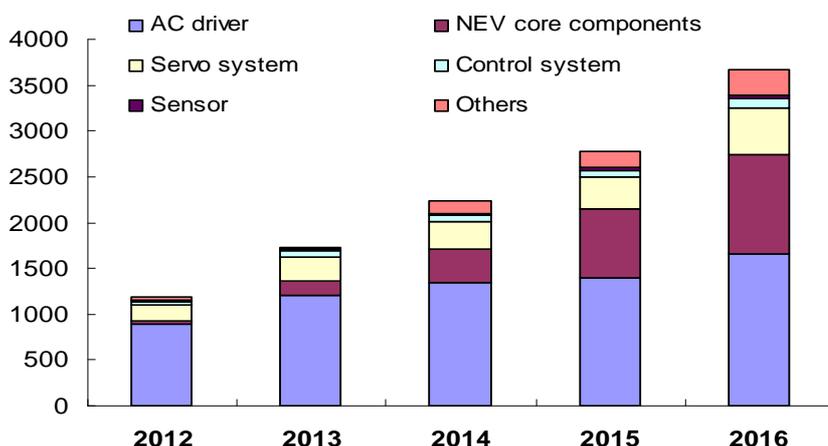
- 1) intelligent equipment & industrial robot core components such as various variable-frequency drive, servo system, control system, industrial vision system and sensor,
- 2) new energy vehicle power assembly core components such as various motor controller and auxiliary power system,
- 3) rail transit traction and control system such as traction converter, auxiliary converter, high-voltage compartment, traction motor and TCMS,
- 4) industrial Internet solutions in the Auto Aftermarket such as intelligent hardware and information management platform.

The proportions of the company's several categories of products to revenue are as follows: the inverter for 45%, the servers for 16%, the new energy products for 23%, the rail traffic for 6.3%, others for 8%.

### Rapid Growth for 10 Years and the Market Share Keeping Increasing

Originally a producer of variable-frequency drive, the Company superimposed grasp of market opportunities and asset acquisitions onto the upgraded core technical strength based on the continuous R&D investment and continued to expand the business scope and the market share. The Company successively developed the general variable-frequency drive, elevator integration machine, servo drive, new energy vehicle electronic control system, rail transit traction system and the industrial robot. In the industrial automation products, the Company is the largest supplier of low- and medium-voltage inverter and servo system. The market share of the low-voltage inverter, the start-up product of the Company, rose from the 13th place (1.8%) in 2008 to the third place in 2016 (6%), only second to ABB and Siemens, and it was the leader in self-owned brands. In the elevator industry, the Company has become the leading elevator integration controller supplier; in the field of the new energy vehicles, the Company has become the leading enterprise of China's new energy vehicle motor controller and is the exclusive supplier of electronic control system of Yutong Bus.

### Revenue breakdown by segments



Source: Company, Phillip Securities Hong Kong Research

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## Buy (Initiation)

CMP: CNY 23.71

(Closing price as at 17 July 2017)

TARGET: CNY 32.40 (+37%)

### COMPANY DATA

O/S SHARES (MN) :	1283
MARKET CAP (CNY MN) :	39480
52 - WK HI/LO (CNY):	25.9/ 17.26

### SHARE HOLDING PATTERN, %

Shenzhen inovance investment ltd	18.63
Mr Zhu	5.56

### PRICE VS. SHCOMP



Source: Phillip Securities (HK) Research

### KEY FINANCIALS

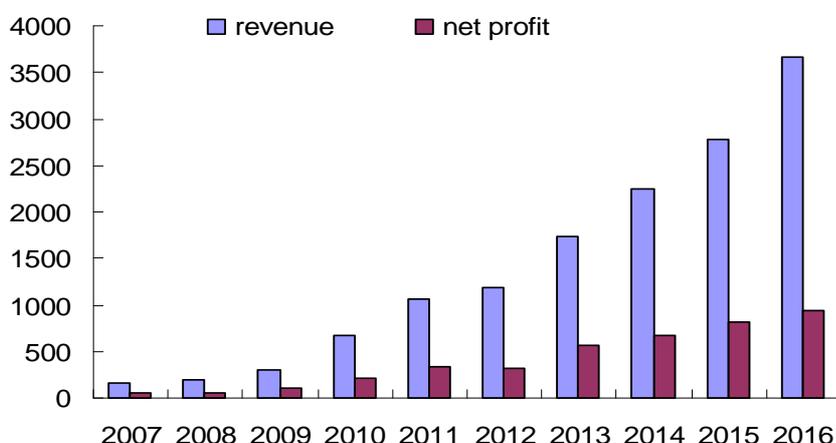
CNY mn	FY15	FY16	FY17E	FY18E
Net Sales	2771	3660	4708	5836
Net Profit	809	932	1179	1491
EPS, CNY	1.02	0.56	0.71	0.90
P/E, x	23.3	42.2	33.5	26.5
BVPS, CNY	5.10	2.84	3.25	3.81
P/BV, x	4.6	8.3	7.3	6.2
DPS (CNY)	0.05	0.28	0.33	0.40
Div. Yield (%)	0.2%	1.2%	1.4%	1.7%

Source: Company reports, Phillip Securities Est.

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The management of the Company attaches great importance to R&D. The high investment continues and more excellent talents are attracted in the meantime. From 2013 to 2016, the investment in R&D of the Company accounted for 9%, 10%, 9% and 11%, respectively of the revenue, and the proportion of the R&D personnel was 23%, 24%, 24% and 28%, respectively. As of the end of 2016, it owned 630 patents with certificates, including 182 patents for invention, 367 utility models and 81 design patents. Since the listing, the Company has launched three equity incentive programs, respectively granting stock options to 227, 174 and 652 people, among which the third one is of the largest range. It nearly covered all the core leaders of the middle and high level, which helped to stimulate the enthusiasm and motivation of the staff. In addition, the sales model of the Company is flexible. The distribution model is for the general products, and the direct sales model is for the important customers. The Company attaches importance to the coordination and cooperation in the sales with the local distributors.

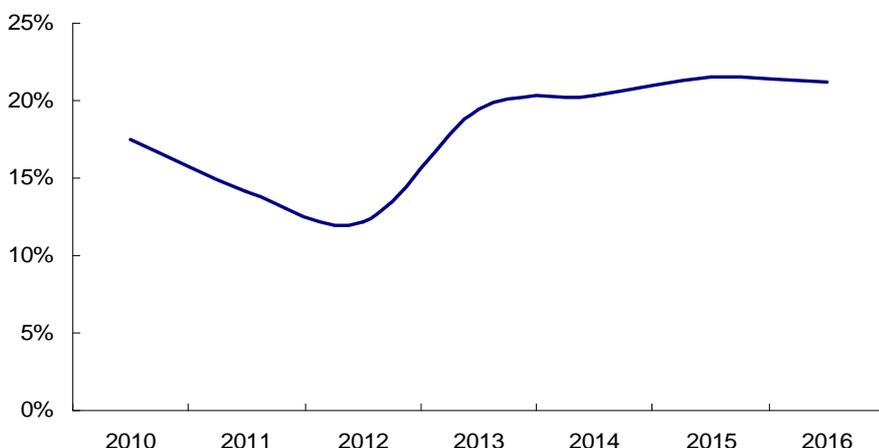
**Top line and bottom line of Company**



Source: Company, Phillip Securities Hong Kong Research

The Company maintained a compound growth rate of revenue up to 41.7% and a compound growth rate of net profit up to 39.1% from 2007 to 2016. The strength of the Company's core R&D ensured that the gross profit margin remained around at a high rate of 50% and that the net interest rate remained at around 30%; what's more, ROE increased from 9.6% in 2007 to 19.8% in 2016. Debt asset ratio of the company is 37.5% with good cash condition.

**ROE trend of Company**



Source: Company, Phillip Securities Hong Kong Research

### **The original business has recovered and the new business turns on the high-speed channel**

The company realized revenue of RMB3.66 billion Yuan in 2016, increasing by 32.11% over the same period of last year. The net profit attributable to the shareholders of the listed company was RMB0.923 billion, up by 15.14% year on year. The net profit growth was faster but still slower than the income growth. It lay in that the proportion of new acquisition rail transportation business of lower gross margin increased while the research and development, management and labor costs increased rapidly. The company realized an income of RMB0.782 billion in 2017, a year-on-year increase of 37.7%; net profit attribution stood at RMB0.172 billion, a year-on-year increase of 23.54%. Gross profit margin fell by 1.55 percentage points to 46.6%, mainly due to China's new energy vehicle market influenced by policy interference in the first quarter.

As fluctuations in the manufacturing and real estate, the profit growth ratio of the company's original business in 2012 and 2014 slowed down, but we agreed that China's manufacturing industry began to enter into the structural pick-up cycle after years of de-stocking and adjusting structure, providing a support for structural recovery of the equipment manufacturing industry. On the other hand, the upgrading of manufacturing transformation and the increase of labor cost will lead to the growth of automation and intelligent equipment demand, thus driving the shipments of company's general automation business. In the main tone of the country striving to develop new energy vehicles and rail transit, the core technology advantages previously accumulated will bring a high-speed development space for new energy motor control products and rail transit traction products. And we believe that from the second half of 2017, factors of perturbing gross profit margin to decline brought by new business will gradually vanish. The company's performance will return to high growth

### **Valuation**

As analyzed above, we expected diluted EPS of the Company to RMB 0.71 and 0.9 of 2017/2018. And we accordingly gave the target price to 32.4, respectively 36x P/E for 2018. "Buy" rating. (Closing price as at 17 July 2017)

## Financials

FYE DEC	FY14	FY15	FY16	FY17F	FY18F
<b>Valuation Ratios</b>					
P/E (X), adj.	27.8	23.3	42.2	33.5	26.5
P/EBITDA	31.0	25.8	42.6	34.1	27.3
P/B (X)	5.4	4.6	8.3	7.3	6.2
Dividend Yield (%)	2.1%	0.2%	1.2%	1.4%	1.7%
<b>Per share data (RMB)</b>					
EPS, (Basic)	0.85	1.02	0.56	0.71	0.90
EPS, (Diluted)	0.85	1.02	0.56	0.71	0.90
DPS	0.50	0.05	0.28	0.33	0.40
BVPS	4.43	5.10	2.84	3.25	3.81
EBITDA/Share	0.77	0.92	0.56	0.69	0.87
<b>Growth &amp; Margins (%)</b>					
<b>Growth</b>					
Revenue	29.9%	23.5%	32.1%	28.6%	24.0%
EBIT	21.2%	22.5%	22.3%	28.5%	28.6%
Net Income, adj.	19.0%	21.4%	15.1%	26.5%	26.4%
<b>Margins</b>					
Gross margin	49.3%	47.5%	47.1%	47.6%	48.1%
EBIT margin	24.8%	24.6%	22.8%	22.8%	23.6%
Net Profit Margin	29.7%	29.2%	25.5%	25.0%	25.5%
<b>Key Ratios</b>					
ROE	20.4%	21.5%	21.2%	23.3%	25.4%
<b>Income Statement (RMB mn)</b>					
<b>Revenue</b>	<b>2243</b>	<b>2771</b>	<b>3660</b>	<b>4708</b>	<b>5836</b>
<b>Gross profit</b>	<b>1107</b>	<b>1316</b>	<b>1724</b>	<b>2239</b>	<b>2807</b>
EBIT	556	681	833	1071	1377
Profit before tax	776	905	1044	1326	1672
<b>Tax</b>	<b>85</b>	<b>71</b>	<b>64</b>	<b>86</b>	<b>105</b>
Profit for the period	690	834	980	1240	1567
Minority interests	24	25	48	61	76
Total capital share	783	795	1660	1665	1665
<b>Net profit</b>	<b>667</b>	<b>809</b>	<b>932</b>	<b>1179</b>	<b>1491</b>

Source: PSR

(Financial figures as at 17 July 2017)

**PHILLIP RESEARCH STOCK SELECTION SYSTEMS**

Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within $\pm$ 5% from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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