

Inovance Technology (300124.CH)

New energy and rail transit services setting out again

China | Automobile Components | Company Updates

Investment Summary

The fluctuation of NEV bus sector affected the Company's 2017 result, But we expect that in 2018, the trend of high growth in China's industrial control industry will continue and the Company's industrial automation services are expected to continue growing rapidly. Meanwhile, the rail transit business will enter a cashing period. As for valuation, we expected diluted EPS of the Company to RMB 0.80 and 0.97 of 2018/2019. And we accordingly gave the target price to RMB32.55, respectively 40.5/33.5x P/E for 2018/2019. "Accumulate" rating. (Closing price as at 4 July 2018)

With a Rapid Growth of Revenue, a Good Situation of Steady Improvement of Net Profits Ongoing

Inovance Technology, with a revenue of RMB4.777 billion in 2017, up 30.5% yoy, with net profits attributable to shareholders up 13.8% yoy to RMB1.06 billion, with EPS RMB0.64 reported, has a result slightly less than our expectation, mainly due to a higher degree of impact on the market of new energy buses by policy adjustment than expectation; the integrated gross margin is 45.12%, down 3 pts yoy, mainly attributable to such reasons as change in business structure, intensified market competition and rise in prices for part of raw materials. Period cost rate rises 2.3 pts, mainly due to enhancing the R&D construction for new business.

In the first quarter of 2018, the Company's revenue has risen by 24.7% yoy to RMB975 million, with net interests attributable to shareholders up 13.9% to RMB196.5 million, EPS RMB0.12 reported. In respect of gross margin, the Company, through constantly strengthening R&D of core technology, continues to launch new products with high gross margin rate as well as in-depth solutions to the industry, so as to keep a steady integrated gross margin for products from the Company and make the decrease of gross margin slow down by 1 pts to 45.54%.

Strong recovery of industrial control services

From product structure, the Company has different progress in each business: Based on data from www.gongkong.com, in 2017, the size of China's industrial automation market increased by 16.5% yoy, in which frequency converter products increased by about 13% yoy, PLC&HMI products by more than 20% yoy, and motion control products by more than 25% yoy. Benefiting from a structural recovery of China's equipment manufacturing and project-based market, the Company's industrial automation services, depending on excellent solutions and brand influence, achieved a market performance of high quality in 2017, with revenues from frequency converter category/servo category/control technology category rising 34%/86%/96% yoy respectively in 2017, their gross margin rates rising -2.7/-0.6/0.95 pts yoy respectively.

In 2017, global robot industry presented a situation of high-speed development, with a constant expansion of industrial scale and market space, and in Chinese market, industrial robots have sales of 136,000 units, with a yoy growth of 60%. The Company's industrial robot products have achieved bulk sales in mobile phone manufacturing and other industries. In addition, Industrial Robots, Nanjing Inovance (industrial vision), and Shanghai LAIEN (high-precision guide screws) had RMB83 million revenue recorded in total, up 1.84 times yoy.

6 July 2018

Accumulate (Downgrade)

CMP CNY 30.79

(Closing price as at 4 July 2018)

TARGET CNY 32.55 (+5.7%)

COMPANY DATA

O/S SHARES (MN) :	1664
MARKET CAP (CNY MN) :	51240
52 - WK HI/LO (CNY):	36.16/ 23.37

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	FY16	FY17	FY18E	FY19E
Net Sales	3660	4777	6306	7988
Net Profit	932	1060	1337	1615
EPS, CNY	0.56	0.64	0.80	0.97
P/E, x	42.2	37.2	29.5	24.4
BVPS, CNY	2.84	3.27	3.84	4.51
P/BV, x	8.3	7.3	6.2	5.3
DPS (CNY)	0.28	0.30	0.39	0.45
Div. Yield (%)	1.2%	1.3%	1.6%	1.9%

Source: Company reports, Phillip Securities Est.

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We expect that in 2018, the trend of high growth in China’s industrial control industry will continue. Meanwhile, we argue that the potential of application market for China’s industrial robots is gradually entering a stage of rapid release, with the yoy growth rate of industrial robot market able to reach 40%, and the Company’s industrial automation services are expected to continue growing rapidly. In 2017, new orders for the Company’s intelligent equipment & robots reached RMB4.56 billion, up 43.4% yoy. In the first quarter of 2018, new orders of the Company had an amount of RMB1.158 billion, up 29.7% yoy.

New energy and rail transit services setting out again

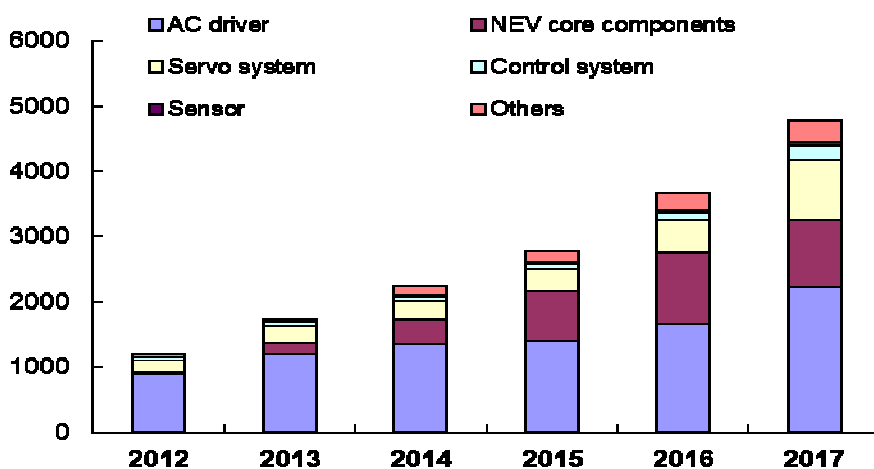
The Company’s new energy & rail transit services had a revenue in 2017 down 6% yoy, with gross margin descending 8 ppts, mainly due to a subsidy policy adjustment to new energy buses. In 2017, the market of new energy buses in China declined sharply by 14%. Suffering from sales down 7.4% of Yutong Bus, a major customer, the Company’s revenue from new energy buses emerge on a decline therefore, but the Company’s new energy logistics van services start bulk sales, which offset part of negative effect. We estimate that, with an end of the transitional period of subsidy policy, new energy bus services in Inovance will step out of bottom, while new energy logistics van services will see a burst development.

For the reasons of the construction period and revenue recognition for subway project, in 2017, the Company’s rail transit services had a revenue only recognized as RMB100 million, down 56% yoy. At present, the Company has more than 1.3 billion orders for rail transit in hand, and with the delivery of projects and revenue recognition, it is estimated that the Company will have its revenue from rail transit reach about RMB530 million, RMB630 million and RMB700 million respectively in the following three years, which will strongly boost the growth of its result.

Valuation

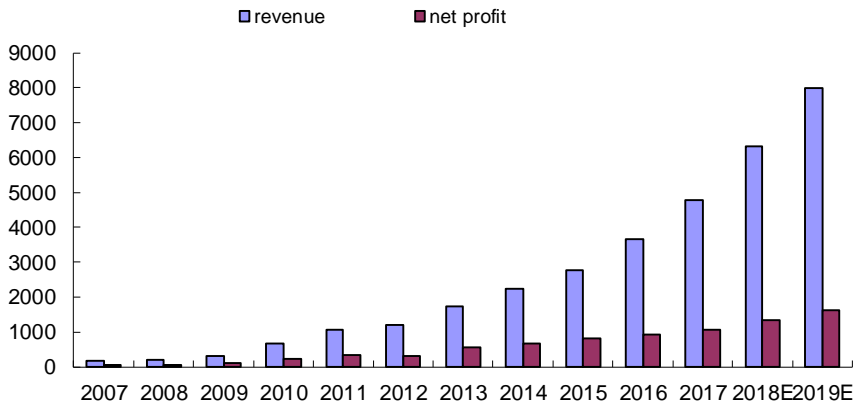
As analyzed above, we expected diluted EPS of the Company to RMB 0.80 and 0.97 of 2018/2019. And we accordingly gave the target price to RMB32.55, respectively 40.5/33.5x P/E for 2018/2019. "Accumulate" rating.

Revenue breakdown by segments



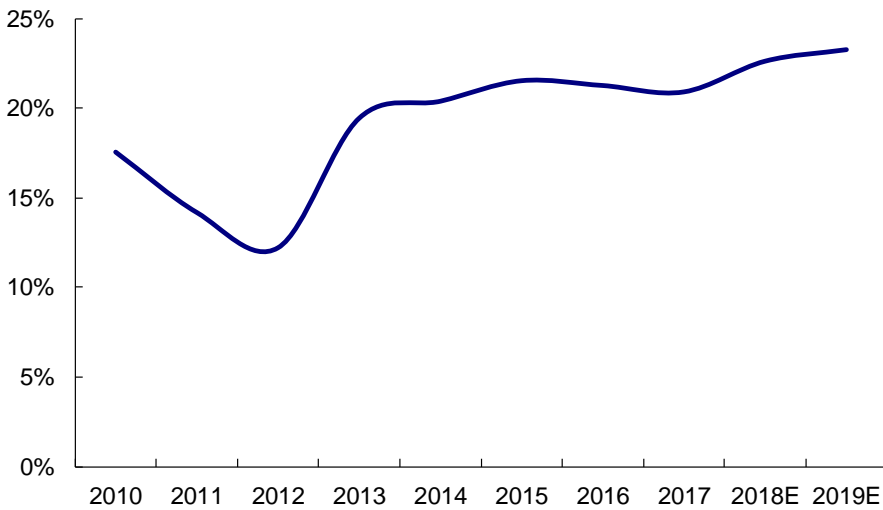
Source: Company, Phillip Securities Hong Kong Research

Top line and bottom line of Company



Source: Company, Phillip Securities Hong Kong Research

ROE trend of Company



Source: Company, Phillip Securities Hong Kong Research

Valuation trend



Source: Bloomberg, Phillip Securities Hong Kong Research

Financials

FYE DEC	FY14	FY15	FY16	FY17	FY18F	FY19F
Valuation Ratios						
P/E (X), adj.	36.1	30.3	54.8	48.3	38.3	31.7
P/EBITDA	40.2	33.5	55.3	55.3	40.7	33.0
P/B (X)	6.9	6.0	10.8	9.4	8.0	6.8
Dividend Yield (%)	1.6%	0.2%	0.9%	1.0%	1.3%	1.5%
Per share data (RMB)						
EPS, (Basic)	0.85	1.02	0.56	0.64	0.80	0.97
EPS, (Diluted)	0.85	1.02	0.56	0.64	0.80	0.97
DPS	0.50	0.05	0.28	0.30	0.39	0.45
BVPS	4.43	5.10	2.84	3.27	3.84	4.51
EBITDA/Share	0.77	0.92	0.56	0.56	0.76	0.93
Growth & Margins (%)						
Growth						
Revenue	29.9%	23.5%	32.1%	30.5%	32.0%	26.7%
EBIT	21.2%	22.5%	22.3%	-1.5%	38.8%	23.8%
Net Income, adj.	19.0%	21.4%	15.1%	13.8%	26.1%	20.8%
Margins						
Gross margin	49.3%	47.5%	47.1%	44.2%	44.6%	44.3%
EBIT margin	24.8%	24.6%	22.8%	17.2%	18.1%	17.7%
Net Profit Margin	29.7%	29.2%	25.5%	22.2%	21.2%	20.2%
Key Ratios						
ROE	20.4%	21.5%	21.2%	20.9%	22.6%	23.2%
Income Statement (RMB mn)						
Revenue	2243	2771	3660	4777	6306	7988
Gross profit	1107	1316	1724	2109	2811	3536
EBIT	556	681	833	821	1140	1411
Profit before tax	776	905	1044	1202	1527	1833
Tax	85	71	64	111	151	174
Profit for the period	690	834	980	1091	1376	1659
Minority interests	24	25	48	31	39	44
Total capital share	783	795	1660	1664	1664	1664
Net profit	667	809	932	1060	1337	1615

Source: PSR

(Financial figures as at 4 July 2018)

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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