

ChinaSoft International (354.HK)

Annual result in line with expectations, emerging business becomes the new growth driver

Hong Kong | TMT | Company Report

29 March 2019

Investment Summary

ChinaSoft International is one of the leading software and information services companies in China. Revenue growth in line with our expectations, while net profit surpassed it. And, emerging business became the new growth driver. Based on 2019 net profit, we assume a P/E ratio of 16.5x (average over the past three years), deriving a TP of HK\$6.57, 22.3% higher than previous TP, we reiterate a “Buy” rating with a potential return of approximately 41.0%. (Closing price at 27 Mar 2019)

Annual result update

Revenue growth in line with our expectations, while net profit surpassed it

The total revenue in 2018 reached RMB 10.6 billion, increased by 14.5% YoY; the net profit attributable to the shareholders was RMB 715.8 million, up by 26.6% YoY. The gross profit margin improved from 29.8% to 30.7%, thanks the increasing portion of emerging business that has higher gross profit margin.

The revenue was generally in line with our expectation, just 0.9% lower, but the gross profit margin was slightly lower than expected, 0.3%. The net profit was above our estimate, about 7%, thanks to the lower administration cost and tax expenses that are deducted on certain research and development expenses.

Demand from Large-sized customers remains strong, but that from small and medium-sized customers became stagnant

The revenue from Technology Professional Services Group (TPG) grew by 16.7% to RMB 9.2 billion, thanks to the strong demand from large-sized customers. The revenue from the largest customers (Huawei) increased by 15.3% to RMB 5.6 billion, accounted for 53.1% of the total revenue. Meanwhile, the revenue growth from HSBC and Ping An were around 47% and 40% respectively. We believe it shows the fact that the large-sized customers are less sensitive to the economic cycle, which will remain the main driver of the Group during the economic downturn.

However, the revenue from Internet IT Services Group (IIG) just grew by 1.8%. The tiny growth was attributed to the pessimistic outlook of the economy, leading to a reduction in IT expenditure from small and medium-sized customers.

Buy

CMP HKD 4.66

(Closing price at 27 March 2019)

TARGET HKD 6.57 (+41.0%)

COMPANY DATA

O/S SHARES (MN) :	2,466
MARKET CAP (HKDMN) :	11,493
52 - WK HI/LO (HKD):	7.72 / 3.45

SHARE HOLDING PATTERN , %

Mr. Chen Yuhong	16.35
UBS Group AG	9.33
CSI Profit Share Scheme	5.54

PRICE PERFORMANCE , %

	1M	3M	1Y
Chinasoft Int'l	-2.31	24.93	-32.95
HSI	-0.15	12.64	-4.31

RETURN VS. HSI



Source: Aastocks, Phillip Securities (HK) Research

KEY FINANCIALS

RMB mn	FY17	FY18	FY19F	FY20F
Revenue	9,244	10,585	12,155	13,885
Net Profit	561	716	821	971
EPS, RMB	0.191	0.235	0.281	0.352
PER, x	17.13	13.08	11.71	10.05
BVPS, RMB	2.15	2.42	2.80	3.24
P/BV, x	1.88	1.67	1.44	1.24
ROE, %	12.0	13.7	13.2	13.3

Source: Company reports, Phillip Securities Est.

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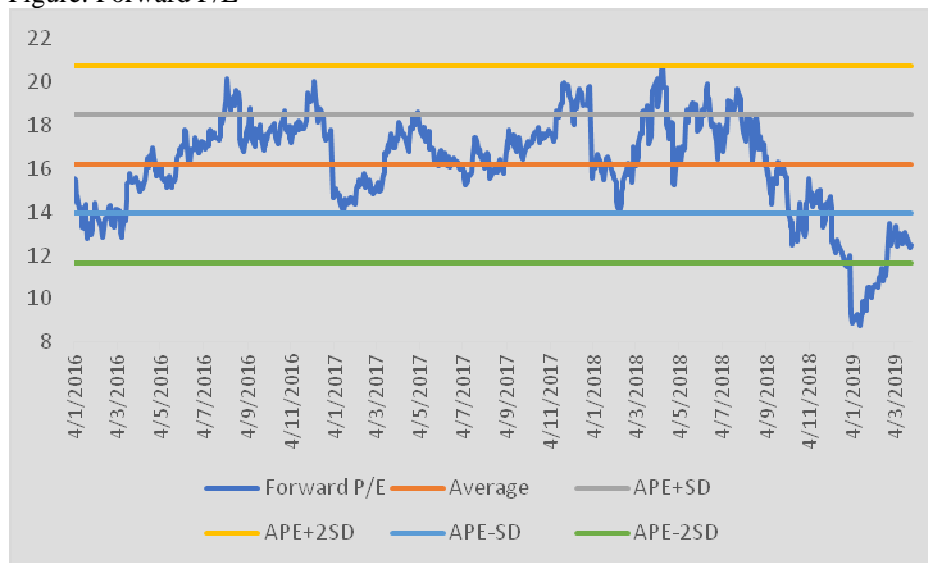
Fast-growing emerging business became an new growth driver

The revenue from Cloud, Big data and Jointforce has reached around RMB 1.6 billion, up by 60% YoY, becoming the new growth driver for the Group. For Cloud Software Park, it is covering 15 cities in 11 provinces, including Jiangsu, Shandong, Hubei, Anhui and so on. For Cloud Integration Platform, the registration from government units exceeded 3,000 with 263 number of projects and the amount was above RMB 137 million. For Jointforce, the number of clients placing packages in the platform has grown by 83% to around 55,000. Since the emerging business has a higher gross margin and create a strong switching cost, we believe the valuation will be enhanced as the proportion of those businesses goes up.

Valuation

We expect the revenue growth of TPG to be 16.5% in 2019, in line with last year, while that of IIG will revive to 4%. Meanwhile, emerging business will remain fast-growing, about 50%. Based on 2019 net profit, we assume a P/E ratio of 16.5x (average over the past three years), deriving a TP of HK\$6.57, 22.3% higher than previous TP, we reiterate a “Buy” rating with a potential return of approximately 41.0%. (HKD/CNY=0.8655)

Figure: Forward P/E



Source: Bloomberg, Phillip Securities (HK) Research

Risk

1. Slower-than-expected growth in SaaS market
2. Suddenly loss on major customers
3. Slower-than-expected growth in emerging business
4. New products replace the company's existing products

Financials

FYE DEC	FY15	FY16	FY17	FY18	FY19F	FY20F
Valuation Ratios						
P/E (X), adj	29.77	21.11	17.13	13.08	11.71	10.05
P/B (X)	2.57	2.19	1.88	1.67	1.44	1.24
Dividend Yield (%)	N/A	0.3%	0.4%	0.5%	0.5%	0.6%
Per share data (RMB)						
EPS, (Basic)	0.136	0.191	0.235	0.308	0.345	0.401
EPS, (Diluted)	0.132	0.184	0.216	0.274	0.306	0.356
DPS (HKD)	N/A	0.012	0.018	0.0215	0.0241	0.0281
BVPS	1.57	1.84	2.15	2.42	2.80	3.24
Growth & Margins (%)						
Growth						
Revenue	15.8%	32.3%	36.3%	14.5%	14.8%	14.2%
EBIT	34.3%	21.0%	18.0%	20.0%	19.1%	17.4%
Net Profit	30.5%	23.1%	37.0%	27.6%	14.6%	18.2%
Margins						
Gross margin	29.7%	29.7%	29.8%	30.7%	31.5%	32.4%
EBIT margin	10.0%	9.1%	7.9%	8.3%	8.6%	8.8%
Net Profit Margin	6.5%	6.0%	6.1%	6.8%	6.8%	7.0%
Key Ratios						
ROA	5.7%	6.0%	7.0%	7.4%	7.3%	7.4%
ROE	9.8%	11.8%	12.0%	13.7%	13.2%	13.3%
Income statement (RMB mn)						
Revenue	5,129	6,783	9,244	10,585	12,155	13,885
Gross Profit	1,523	2,016	2,750	3,245	3,825	4,497
EBIT	513	620	732	878	1,047	1,228
EBT	420	525	633	760	912	1,078
Net Profit	333	410	561	716	821	971
Minority Interest	53	(32)	(4)	(44)	(29)	(19)
Net profit for owners	280	442	566	760	850	990

Source: Company, Phillip Securities (HK) Research

Exchange rate (0.8655) is HKDCNY1Y forward contract price on March 27 from Wind.

(Financial figures as at 27 March 2019)

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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