

# Inovance Technology (300124.CH)

## 2019 Q1 is Likely to Be a Low Point for Result

China | Automobile Components | Company Updates

27 May 2019

### Investment Summary

#### Revenue Grows Rapidly and Net Profits Increase Steadily in 2018

In 2018, Inovance Technology reported net profits of RMB1.167 billion attributable to shareholders of the parent company, up 10.1% yoy, with EPS of RMB0.70 and dividends per share of RMB0.2. The result is lower than our expectations, mainly because 1) domestic macroeconomic downturn in the fourth quarter of last year affected downstream demand, 2) new energy bus market in the reporting period is still affected by the policy adjustment. The duration is longer than expected. However, by virtue of the Company's competitive advantages in many segments and the delivery of rail transit orders in the early stage, the Company's overall revenue still achieved rapid growth, with the annual revenue of RMB5.874 billion, up by 23% yoy.

In terms of business, the revenue of the general segment reached RMB2.587 billion, up by 32% yoy. The elevator business reported revenue of RMB1.37 billion, up 22.34% yoy. Electro-hydraulic servo business reported revenue of RMB495 million, up 3% yoy. The new energy vehicle business reported revenue of RMB841 million, down 8% yoy. Rail transit revenue reached RMB212 million, up 112% yoy.

In 2018, the Company's overall gross margin was 41.81%, down by 3.31 ppts yoy, mainly due to changes in the Company's product revenue structure and intensified industrial competition in 2018: (1) the price reduction of Yutong bus, the main customer, led to a decrease of 10.56 ppts in the gross margin of the new energy sector; (2) the sales structure of elevator business has declined, the market competition of automation business has intensified, and the gross margin has declined slightly.

The Company has a good cost control, and its period cost rate is 25.46% (saving 0.96 ppts yoy), among which the proportion of research and development expenses is 12.12% (reducing 0.28 ppts yoy), still maintaining a high level of research and development expenditure. By the end of 2018, the Company has completed eight designated projects of domestic auto companies. In 2019, with the gradual increase of designated models, the electric motor control business of the Company's passenger cars will start to enter a period of high growth.

#### Q1 of 2019 is Likely to Be a Low Point for Result

In Q1 of 2019, the Company reported revenue of RMB1.10 billion, up 12.8% yoy, and net profit of RMB129 million, down 34.3% yoy. 2019 Q1 results fell, mainly because: 1. The decline in the revenue structure and increased competition in the industry reduced gross margin by 4.13 ppts yoy. 2. The amount of VAT software rebate received was reduced, resulting in a yoy decline of 46.77% in other income. 3. During the reporting period, the increase of personnel and the implementation of equity incentive led to the increase of expenses. 4. Exchange rate fluctuations led to increased investment losses in Qianhai Jingrui Hehui Financial Services Co., LTD. However, operating cash flow improved in Q1, from the outflow of RMB94 million to the inflow of RMB21 million in the same period of last year.

In terms of business, sales revenue of automation business reported RMB503 million, up by 5.2% yoy. The integrated elevator business reported sales revenue of RMB241 million, up 12.35% yoy. Electro-hydraulic servo business and Yishitong business reported revenue of RMB106 million, down 14.59% yoy. Revenue from new energy vehicles reported RMB75 million, down 8.8% yoy. Rail transit business reported revenue of RMB83 million, up 65% yoy. Industrial robot business reported revenue of RMB21 million, up 38.5% yoy.

### Buy (Upgrade)

CMP CNY 22.94

(Closing price as at 23 May 2019)

TARGET CNY 28.41 (+23.8%)

#### COMPANY DATA

O/S SHARES (MN) :	1664
MARKET CAP (CNY MN) :	38125
52 - WK HI/LO (CNY):	34.15/ 19.01

#### 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	FY17	FY18	FY19E	FY20E
Net Sales	4777	5874	7402	9441
Net Profit	1060	1167	1356	1683
EPS, CNY	0.64	0.70	0.81	1.01
P/E, x	36.0	32.7	28.2	22.7
BVPS, CNY	3.27	3.75	4.46	5.17
P/BV, x	7.0	6.1	5.1	4.4
DPS (CNY)	0.30	0.20	0.26	0.31
Div. Yield (%)	1.3%	0.9%	1.1%	1.4%

Source: Company reports, Phillip Securities Est.

Research Analyst  
**Zhangjing**  
 (+ 86 51699400-103)

zhangjing@phillip.com.cn

### Acquisition of BST Opens up Overseas Markets

Recently, the Company announced that it planned to acquire 100% of BST by means of cash and equity, with a total transaction amount of RMB2.487 billion, corresponding to PS\PE\PB of 1.03, 10.57, 4.57 times. BST is a quality elevator parts supplier mainly serving foreign customers. BST's man-machine interface interaction system, wire and cable system, and other products are in a leading position among international brands of elevator manufacturers. It has stable cooperative relations with most of the world famous elevator manufacturers, including Otis, Kone, thyssenkrupp, Schindler and Fujitec, and has entered the global supplier system of some of them. Inovance Technology and BST are complementary to each other in terms of customers and products, with obvious synergies. By opening up the overseas market through BST, we will further expand the scale of overseas business and expand business development space.

### Investment Thesis

By the end of 2018, the Company had accumulated RMB1.38 billion of orders in hand, and the electric motor control business of passenger cars will gradually improve in 2019. The industrial control industry is expected to gradually bottom out and recover as PMI returns to above the 50-point line delineating growth from contraction. By opening up overseas elevator market, and the Company's result in 2019 is expected to grow steadily.

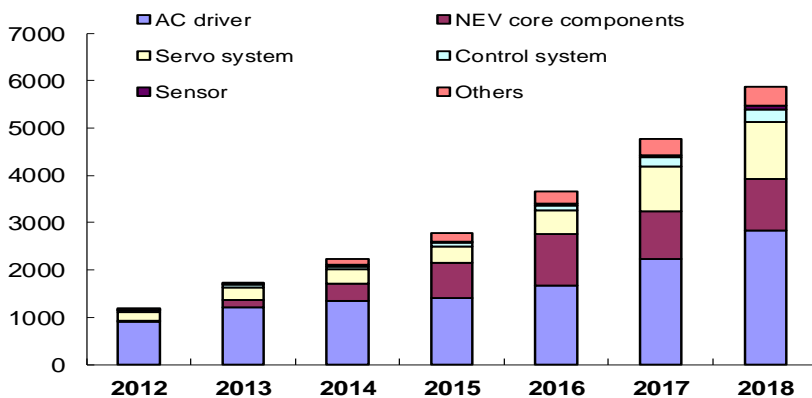
As for valuation, we expected diluted EPS of the Company to RMB 0.81 and 1.01 of 2019/2020. And we accordingly gave the target price to RMB28.41, respectively 35/28x P/E for 2019/2020. "Buy" rating. (Closing price as at 23 May 2019)

### Valuation trend



Source: Bloomberg, Phillip Securities Hong Kong Research

### Revenue breakdown by segments



Source: Company, Phillip Securities Hong Kong Research

## Financials

FYE DEC	FY15	FY16	FY17	FY18	FY19F	FY20F
<b>Valuation Ratios</b>						
P/E (X), adj.	22.5	40.9	36.0	32.7	28.2	22.7
P/EBITDA	24.9	41.2	41.2	36.5	31.2	24.2
P/B (X)	4.5	8.1	7.0	6.1	5.1	4.4
Dividend Yield (%)	0.2%	1.2%	1.3%	0.9%	1.1%	1.4%
<b>Per share data (RMB)</b>						
EPS, (Basic)	1.02	0.56	0.64	0.70	0.81	1.01
EPS, (Diluted)	1.02	0.56	0.64	0.70	0.81	1.01
DPS	0.05	0.28	0.30	0.20	0.26	0.31
BVPS	5.10	2.84	3.27	3.75	4.46	5.17
EBITDA/Share	0.92	0.56	0.56	0.63	0.74	0.95
<b>Growth &amp; Margins (%)</b>						
<b>Growth</b>						
Revenue	23.5%	32.1%	30.5%	23.0%	26.0%	27.6%
EBIT	22.5%	22.3%	-1.5%	9.9%	17.9%	30.9%
Net Income, adj.	21.4%	15.1%	13.8%	10.1%	16.2%	24.1%
<b>Margins</b>						
Gross margin	47.5%	47.1%	44.2%	41.0%	41.3%	40.4%
EBIT margin	24.6%	22.8%	17.2%	15.4%	14.4%	14.8%
Net Profit Margin	29.2%	25.5%	22.2%	19.9%	18.3%	17.8%
<b>Key Ratios</b>						
ROE	21.5%	21.2%	20.9%	20.0%	19.8%	21.0%
<b>Income Statement (RMB mn)</b>						
Revenue	2771	3660	4777	5874	7402	9441
Gross profit	1316	1724	2109	2411	3055	3814
EBIT	681	833	821	902	1064	1393
Profit before tax	905	1044	1202	1284	1501	1863
Tax	71	64	111	75	98	121
Profit for the period	834	980	1091	1209	1403	1742
Minority interests	25	48	31	42	47	58
Total capital share	795	1660	1664	1664	1664	1664
<b>Net profit</b>	<b>809</b>	<b>932</b>	<b>1060</b>	<b>1167</b>	<b>1356</b>	<b>1683</b>

Source: PSR

(Financial figures as at 23 May 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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**Contact Information (Regional Member Companies)**
**SINGAPORE**
**Phillip Securities Pte Ltd**

250 North Bridge Road, #06-00 Raffles City Tower,  
Singapore 179101  
Tel : (65) 6533 6001 Fax: (65) 6535 3834  
[www.phillip.com.sg](http://www.phillip.com.sg)

**INDONESIA**
**PT Phillip Securities Indonesia**

ANZ Tower Level 23B, Jl Jend Sudirman Kav 33A,  
Jakarta 10220, Indonesia  
Tel (62) 21 5790 0800 Fax: (62) 21 5790 0809  
[www.phillip.co.id](http://www.phillip.co.id)

**THAILAND**
**Phillip Securities (Thailand) Public Co. Ltd.**

15th Floor, Vorawat Building, 849 Silom Road,  
Silom, Bangrak, Bangkok 10500 Thailand  
Tel (66) 2 2268 0999 Fax: (66) 2 2268 0921  
[www.phillip.co.th](http://www.phillip.co.th)

**UNITED STATES**
**Phillip Futures Inc.**

141 W Jackson Blvd Ste 3050  
The Chicago Board of Trade Building  
Chicago, IL 60604 USA  
Tel (1) 312 356 9000 Fax: (1) 312 356 9005

**MALAYSIA**
**Phillip Capital Management Sdn Bhd**

B-3-6 Block B Level 3, Megan Avenue II,  
No. 12, Jalan Yap Kwan Seng, 50450 Kuala Lumpur  
Tel (60) 3 2162 8841 Fax (60) 3 2166 5099  
[www.poems.com.my](http://www.poems.com.my)

**CHINA**
**Phillip Financial Advisory (Shanghai) Co. Ltd.**

No 436 Heng Feng Road, Green Tech Tower Unit 604  
Shanghai 200 070  
Tel (86) 21 5169 9400 Fax: (86) 21 6091 1155  
[www.phillip.com.cn](http://www.phillip.com.cn)

**FRANCE**
**King & Shaxson Capital Ltd.**

3rd Floor, 35 Rue de la Bienfaisance  
75008 Paris France  
Tel (33) 1 4563 3100 Fax : (33) 1 4563 6017  
[www.kingandshaxson.com](http://www.kingandshaxson.com)

**AUSTRALIA**
**PhillipCapital Australia**

Level 10, 330 Collins Street  
Melbourne VIC 3000  
Tel (+61) 3 8633 9803 Fax (+61) 3 8633 9899  
[www.phillipcapital.com.au](http://www.phillipcapital.com.au)

**HONG KONG**
**Phillip Securities (HK) Ltd**

11/F United Centre 95 Queensway Hong Kong  
Tel (852) 2277 6600 Fax: (852) 2868 5307  
[www.phillip.com.hk](http://www.phillip.com.hk)

**JAPAN**
**Phillip Securities Japan, Ltd**

4-2 Nihonbashi Kabutocho, Chuo-ku  
Tokyo 103-0026  
Tel: (81) 3 3666 2101 Fax: (81) 3 3664 0141  
[www.phillip.co.jp](http://www.phillip.co.jp)

**INDIA**
**PhillipCapital (India) Private Limited**

No. 1, 18th Floor, Urmi Estate, 95 Ganpatrao Kadam Marg,  
Lower Parel West, Mumbai 400013  
Tel: (9122) 2300 2999 Fax: (9122) 6667 9955  
[www.phillipcapital.in](http://www.phillipcapital.in)

**UNITED KINGDOM**
**King & Shaxson Ltd.**

6th Floor, Candlewick House, 120 Cannon Street  
London, EC4N 6AS  
Tel (44) 20 7929 5300 Fax: (44) 20 7283 6835  
[www.kingandshaxson.com](http://www.kingandshaxson.com)

**SRI LANKA**
**Asha Phillip Securities Limited**

Level 4, Millennium House, 46/58 Navam Mawatha,  
Colombo 2, Sri Lanka  
Tel: (94) 11 2429 100 Fax: (94) 11 2429 199  
[www.ashaphillip.net/home.htm](http://www.ashaphillip.net/home.htm)