

Kingdee International (268.HK)

The development of cloud business remains good, reason to buy still exists

22 August 2019

Hong Kong | TMT | Company Report

Investment Summary

The revenue in H1 was RMB 1.49 bn, up by 16.1% YoY; the net profit attributable to owners was RMB 109.6 mn, down by 35.4% YoY. The revenue growth in ERP business and Cloud services were 1.2% (below our previous estimate) and 54.9% (in line with our previous estimate). We give a TP of \$8.55, downgrading to “Buy” recommendation, with 10.3% potential upside. (Closing price at 20 Aug 2019)

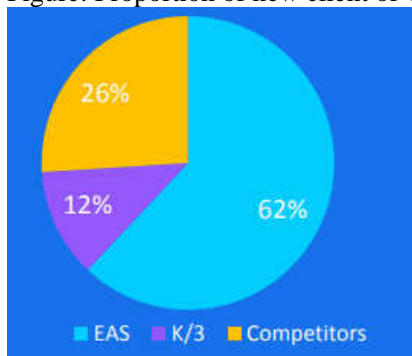
Result update

The revenue in H1 was RMB 1.49 bn, up by 16.1% YoY; the net profit attributable to owners was RMB 110 mn, down by 35.4% YoY. The revenue growth in ERP business and Cloud services were 1.2% (below our previous estimate) and 54.9% (in line with our previous estimate). The GPM dropped from 80.2% to 79.5%. The selling & marketing expenses and research & development cost as pct of revenue increased to 51.4% and 17% respectively, due to the increase in marketing and promotion expenses as well as research and development costs in cloud products. The proportion of cloud service to revenue grew from 27.8% in 18H1 to 37% in 19H1.

Business ERP

The revenue growth from ERP business in 19H1 was 1.2%, lower than our previous estimate 3%. As we mentioned in previous report, we believe the drop in the growth of traditional ERP were 1) the clients delay or reduce its IT expenditure due to the concern on the economic downturn in the first half and 2) the demand of traditional ERP is shifting to Cloud services. 62% and 12% of the cosmic clients are from EAS and K/3, implying that some of the demand on ERP business has been shifted to Cloud services. Also, the management said they will start to encourage their EAS clients moving to Cosmic in the next few year. As a result, we are more conservative on the prospective of the ERP business as the Group place more emphasis on Cloud services.

Figure: Proportion of new client of Cosmic



Source: Company report, Phillip Securities (HK) Research

Accumulate

CMP HKD 7.75

(Closing price at 20 Aug 2019)

TARGET HKD 8.55 (+10.3%)

COMPANY DATA

O/S SHARES (MN) :	3,316
MARKET CAP (HKDMN) :	25,700
52 - WK HI/LO (HKD):	10.96 / 5.50

SHARE HOLDING PATTERN , %

Mr. Xu Shaochun	22.26
The Capital Group Companies, Inc.	10.85

PRICE PERFORMANCE , %

	1M	3M	1Y
Kingdee Int'l	-0.13	-1.77	-4.08
HSI	-7.62	-5.92	-3.39

RETURN VS. HSI



Source: Aastocks, Phillip Securities (HK) Research

KEY FINANCIALS

RMB mn	FY17	FY18	FY19E	FY20E
Revenue	2,303	2,809	3,295	4,079
Net Profit	310	412	309	337
EPS, RMB	0.110	0.125	0.093	0.101
PER, x	63.18	55.72	74.90	68.72
BVPS, RMB	1.44	1.68	1.75	1.85
P/BV, x	4.84	4.15	3.98	3.78
ROE, %	8.2	8.6	5.4	5.6

Source: Company reports, Phillip Securities Est.

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Cloud service

Cosmic

Cosmic has acquired 28 new clients in 19H1, where the total contract size reached RMB 33mn, representing an average contract size of RMB 1.2 mn. Their new clients included Xiamen C&D, Hesteel Group, Xiwang Group and etc. Only RMB 15 mn was recorded in the first half from Cosmic, while the other has been included in contract liabilities. The Group has started its ISV partner plan on the platform of Cosmic in order to create a PaaS ecosystem. The number of verified ISV reached about 50 and expect to be more 100 in the end of 2019. There will still be a huge investment in cosmic, so it is expected a few year will be needed for breakeven.

Galaxy

Galaxy was doing well in the first half, where its customer exceeded 11,500, and 90% of it are new customers, representing a YoY increase of 50%. It has acquired some renowned clients, such as Tencent, Alibaba, Samsung, Huawei and etc. Also, 77% of the new customers are new ERP users and 13% of which are from competitors. The dollar retention rate remained high, at 90%. Galaxy raised its price in this July. The management claimed that the net loss incurred from Galaxy is reducing, only incurred a net loss of RMB 10 mn, and should be able to breakeven in the second half of 2019.

Figure: Cloud Product Information

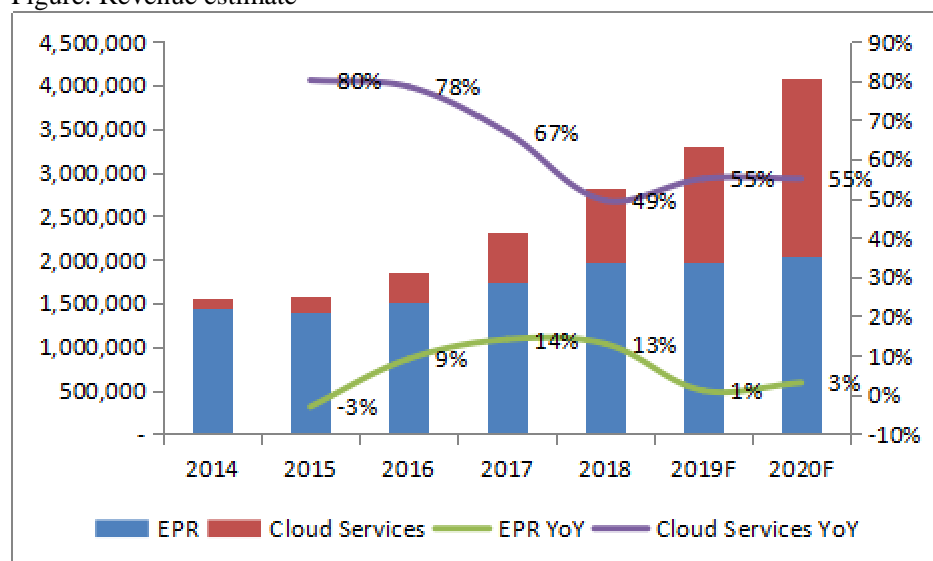
		2015	2016	2017	2018H1	2018H2	2019H1
Galaxy	Paying Users	1,000	2,500	5,500	7,500	9,500	11,500
	YoY		150%	120%	110%	73%	51%
	Customer Retention Rate		90%	90%	80%	80%	80%
	Dollar Retention Rate					95%	90%
Cosmic	No. of customer				15	43	43
Jingdou Cloud	Paying Users	65,000	85,000	150,000	160,000	80,000	95,000
	YoY		31%	76%	28%	60%	65%
	Customer Retention Rate	75%	75%	75%	70%	70%	80%
Guan Yiyun	Paying Users	3,600	5,000	6,200	7,000	7,600	4,500
	YoY		39%	24%	20%	20%	29%
	Customer Retention Rate		N/A	70%	70%	70%	80%

Source: Company report, Phillip Securities (HK) Research

Earnings forecast

In view of the dropped growth in ERP business for the first half, we expect the revenue growth of ERP business will be 1%/3% in 2019F/20F. Besides, we also expect the revenue growth of cloud business will be 55% for both 2019F/20F, as we are optimistic to the SaaS market.

Figure: Revenue estimate



Source: Company report, Phillip Securities (HK) Research

Valuation

We adopted sum of the parts valuation by dividing the business into three parts: 1) Traditional ERP business (P/E), 2) Cloud business (P/S), and 3) Investment real estate business (book valuation). We forecast the earnings per share of the traditional ERP business in 2019F to be RMB 0.106, 2.8% lower than the previous estimate in reflection of the slower growth in the first half, with target PE ratio 15x; the revenue of cloud services per share in 2019F would be RMB 0.397, 3.1% higher than the previous estimate in reflection of the strong growth. We maintain the target PS ratio to be 13x; for the investment real estate business, the book valuation is used, and the valuation per share is RMB 0.55. Finally, a net cash is RMB 0.26 per share in 2018. A target price of HK\$8.55 was derived, 3.9% lower than previous target price. As the stock price has rebounded recently, we downgrade to “Accumulate” recommendation, with 10.3% potential upside. (HKD/CNY: 0.90)

Risk

1. Slower-than-expected growth in cloud products
2. The economy of China slows down
3. Cloud ERP may take away the existing customers of traditional ERP, particularly SME

Financials

FYE DEC	FY15	FY16	FY17	FY18	FY19F	FY20F
Valuation Ratios						
P/E (X), adj	182.59	69.89	63.18	55.72	74.90	68.72
P/B (X)	5.95	5.70	4.84	4.15	3.98	3.78
Dividend Yield (%)	N/A	N/A	0.2%	0.1%	0.1%	0.1%
Per share data (RMB)						
EPS, (Basic)	0.038	0.100	0.110	0.125	0.093	0.101
EPS, (Diluted)	0.036	0.097	0.108	0.123	0.091	0.100
DPS (HKD)	N/A	N/A	0.016	0.011	0.010	0.011
BVPS	1.17	1.22	1.44	1.68	1.75	1.85
Growth & Margins (%)						
Growth						
Revenue	-1.9%	22.8%	23.7%	21.9%	17.3%	23.8%
Operating profit (excluding fair value gains on investment properties)	9.6%	-33.6%	50.8%	25.3%	-9.0%	8.3%
Net Income (excluding gain/loss from discontinued operations)	8.5%	-1.0%	50.4%	26.5%	-23.8%	9.0%
Margins						
Gross margin	80.9%	81.3%	81.5%	81.7%	81.0%	81.0%
Operating profit margin (excluding fair value gains on investment properties)	21.4%	11.5%	14.1%	14.5%	11.2%	9.8%
Net Profit Margin	14.3%	11.6%	14.0%	14.6%	9.5%	8.3%
Key Ratios						
ROE	4.0%	8.5%	8.2%	8.6%	5.4%	5.6%
Income statement (RMB mn)						
Revenue	1,517	1,862	2,303	2,809	3,295	4,079
Gross Profit	1,227	1,514	1,876	2,294	2,669	3,304
EBIT	341	249	421	453	370	400
EBT	280	209	378	448	363	395
Net profit (excluding gain/loss from discontinued operations)	217	215	324	409	312	340
Minority Interest	(0)	1	14	(3)	3	3
Net profit for owners	106	288	310	412	309	337

Source: Company, Phillip Securities (HK) Research

Exchange rate (0.90) is HKDCNY1Y forward contract price on August 20 from Wind.

(Financial figures as at 20 August 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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