

# Inovance Technology (300124 CH)

## 3Q2020 Result Beat, reaffirm accumulate rating

China | Automobile Components | Company Updates

13 November 2020

### Investment Summary

#### Earnings Soared by 132% in the First Three Quarters

In the first three quarters of 2020, the total revenue of Inovance Technology achieved RMB8.098 billion, increasing by 65% yoy. Net profit attributable to the listed company's shareholders hit RMB1.498 billion with a yoy increase of 131.93%. Revenue in Q1, Q2 and Q3 achieved RMB1.55/3.24/3.31 billion with a significant yoy rise of 41%/100%/51%, respectively. The net profits in the first three quarters were RMB170 million, RMB600 million and RMB720 million, a yoy jump of 34%, 123% and 192%, respectively.

The main reasons for the company's good result lie in:

- 1) Inovance Technology has seized the opportunities of strong demands for mask-making machines and melt-blown nonwovens equipment as well as the opportunities of demands for domestic brands due to the insufficient supply of foreign brands during the worldwide pandemic with its revenue of high-margin products including general-purpose servos and control systems soaring.
- 2) Inovance Technology has effectively reduced costs and realized higher efficiency, and its gross margin of the integration of servos, control systems and elevators has increased yoy.
- 3) Inovance Technology has made solid achievements in the resumption of work and production and control over the Covid-19 pandemic.
- 4) Rebates and subsidies of VAT software have been increased. Sales expenses, management expenses and R&D expenses have grown slower than revenue under the economies of scale.
- 5) Last year's performance was at a relatively low point during the adjustment period. Inovance Technology's profitability has improved substantially with the net profit margin in the third quarter up by nearly 10 ppts yoy and 3.4 ppts mom. The company also raised its 2020 goal of net profit attributable to the parent company to a range from RMB1.809 billion to RMB2.285 billion, hitting a yoy increase between 90% and 140%.

#### Many business segments delivered strong momentum

The company has made remarkable achievements in many businesses of departments.

- 1) Inovance Technology has gained approximately RMB3.396 billion from general automation business with a yoy increase of 63.6%. Drawing on the product competitiveness created by active market expansion and continuous R&D investment, the company has fully enjoyed this opportunity of import substitution in the transformation towards high-end manufacturing and localization of downstream equipment. As a result, all segments of its automation business have grown rapidly. We believe that China's industrial automation industry will enjoy a continuously promising future with a projected high-rate growth of over 40% in 2021.
- 2) The revenue of Inovance Technology's elevator business reached RMB3.171 billion with a yoy increase of 82%. The integration effect after the company's acquisition of BST has begun to take effect. To be more specific, its supporting business at a large scale has grown rapidly and the progress of multinational enterprise business projects have fallen in its expectation. With the advancement of the elevator, business is expected to maintain steady growth with the increasing production capacity of the Jiashan base.

### Accumulate (Maintain)

CMP CNY 80.33

(Closing price as at 11 November)

TARGET CNY 87.45 (+9%)

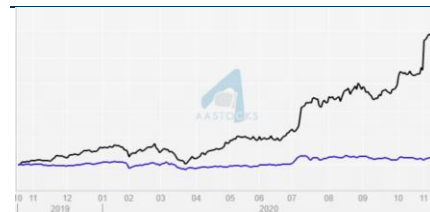
#### COMPANY DATA

O/S SHARES (MN) :	1720
MARKET CAP (CNY MN) :	138145
52 - WK HI/LO (CNY):	83.36/ 23.16

#### SHARE HOLDING PATTERN, %

Shenzhen inovance investment ltd	18.63
Mr Zhu	5.56

#### PRICE VS. SHCOMP



Source: Aastock, Phillip Securities (HK) Research

#### KEY FINANCIALS

CNY mn	FY19	FY20E	FY21E	FY22E
Net Sales	7390	11846	14833	18439
Net Profit	952	2032	2624	3473
EPS, CNY	0.55	1.18	1.53	2.02
P/E, x	146.1	68.0	52.7	39.8
BVPS, CNY	4.98	6.01	8.02	9.09
P/BV, x	16.1	13.4	10.0	8.8
DPS (CNY)	0.18	0.37	0.50	0.63
Div. Yield (%)	0.2%	0.5%	0.6%	0.8%

Source: Company reports, Phillip Securities Est.

#### Research Analyst

ZhangJing (+ 86 021-51699400-103)

zhangjing@phillip.com.cn

3) The revenue of Inovance Technology's new energy vehicle business has reached RMB631 million, increasing 85% yoy, and the gross margin of new energy vehicles has been improved. The passenger car business has seen rapid growth in orders from new car manufacturers, and the logistics car business has grown rapidly. But the passenger car business has relatively declined. At present, at the domestic customer level, the company became a supplier of products including passenger car motors, electronic controls and power supplies for first-line OEMs. These business orders are expected to maintain strong growth momentum next year with an increasing number of domestic new energy vehicles.

4) The industrial robot business (including Shanghai Laien) has scored a sales revenue of RMB120 million, a 71% yoy growth. The company has expanded its downstream businesses with a comprehensive plan for the combination of core components, complete machines, vision and techniques. The remarkable growth in 3C, lithium battery and other industries have been achieved with mass sales being delivered.

5) Inovance Technology's rail transit business has reported the sales revenue of RMB217 million with a yoy decline of 28%. The company has continued to complete new projects and improve the maintenance market in terms of its rail transit business. It has sufficiently stock orders worth around RMB1.1 billion. And the maintenance project of the traction system of Suzhou Metro Line 1 was obtained during the reporting period.

#### Improved gross margin and lower expense ratio

In the first three quarters, the company's comprehensive gross margin was 39.35% growing by 1.08% yoy. The number was 44.23% without consideration of BST's consolidation factors with a yoy increase of 3.08%. And BST's gross margin was 26.08%. The increase in gross margin was mainly due to improvements in product structures, the increase in the proportion of high-margin servos, PLCs and some inverters and the reduction in procurement and manufacturing costs with significant contributions.

The company's expenses growth rate was lower than that of its revenue and its period expense ratio has improved remarkably to 21.15% declining by 6.36 ppts yoy. These achievements were mainly attributed to the scale effect and the initial results for the management reform aiming at lower costs and higher efficiency.

## Investment Thesis

Recent years have seen growing uncertainties worldwide which created great opportunities for import substitution. The demand for domestic industrial automation products has been gradually stimulated by downstream industries such as 3C, new energy, and photovoltaics. The company has recently raised RMB2.1 billion to expand production capacity, increase research and development and implemented equity incentives to enhance future development momentum. We are optimistic about the company's future growth potential as a leader in the industrial automation field with the increasingly obvious growth of its intrinsic value in the long run.

As for valuation, we expected diluted EPS of the Company to RMB 1.18/1.53/2.02 of 2020/2021/2022. And based on 1.5x PEG, we accordingly gave the target price to RMB 87.45, respectively 74/57/43x P/E and 15/11/10.2x P/B for 2020/2021. "Accumulate" rating. (Closing price as at 11 November)

## Valuation trend



Source: Bloomberg, Phillip Securities Hong Kong Research

## Financials

FYE DEC	FY17	FY18	FY19	FY20F	FY21F	FY22F
<b>Valuation Ratios</b>						
P/E (X), adj.	126.1	114.6	146.1	68.0	52.7	39.8
P/EBITDA	144.2	127.8	132.7	62.0	46.8	36.4
P/B (X)	24.6	21.4	16.1	13.4	10.0	8.8
Dividend Yield (%)	0.4%	0.2%	0.2%	0.5%	0.6%	0.8%
<b>Per share data (RMB)</b>						
EPS, (Basic)	0.64	0.70	0.55	1.18	1.53	2.02
EPS, (Diluted)	0.64	0.70	0.55	1.18	1.53	2.02
DPS	0.30	0.20	0.18	0.37	0.50	0.63
BVPS	3.27	3.75	4.98	6.01	8.02	9.09
EBITDA/Share	0.56	0.63	0.61	1.30	1.72	2.21
<b>Growth &amp; Margins (%)</b>						
<b>Growth</b>						
Revenue	30.5%	23.0%	25.8%	60.3%	25.2%	24.3%
EBIT	-1.5%	9.9%	-7.9%	116.3%	33.7%	35.1%
Net Income, adj.	13.8%	10.1%	-18.4%	113.5%	29.1%	32.3%
<b>Margins</b>						
Gross margin	44.2%	41.0%	37.0%	39.0%	39.8%	40.7%
EBIT margin	17.2%	15.4%	11.2%	15.2%	16.2%	17.6%
Net Profit Margin	22.2%	19.9%	12.9%	17.2%	17.7%	18.8%
<b>Key Ratios</b>						
ROE	20.9%	20.0%	12.8%	21.4%	22.3%	24.1%
<b>Income Statement (RMB mn)</b>						
Revenue	4777	5874	7390	11846	14833	18439
Gross profit	2109	2411	2736	4621	5909	7496
EBIT	821	902	830	1796	2401	3245
Profit before tax	1202	1284	1056	2234	2825	3739
Tax	111	75	46	127	161	213
Profit for the period	1091	1209	1010	2106	2664	3526
Minority interests	31	42	58	75	40	53
Total capital share	1664	1664	1732	1720	1720	1720
Net profit	1060	1167	952	2032	2624	3473

Source: PSR

(Closing price as at 11 November)

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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

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