

Fuyao Glass (3606 HK)

Overseas Business Bottomed Out

China | Auto & Parts | Company Update

23 November 2020

Investment Summary

Q3 Results Exceed Expectations

According to Q3 report of Fuyao Glass, during the first three quarters, the Company recorded operating revenue of RMB13.78 billion, down by 11.9% yoy. Net profit attributable to the parent company was RMB1.72 billion, down by 26.6% yoy. The operating revenue of Q3 was RMB5.66 billion, up by 5.8% yoy. Net profit attributable to the parent company was RMB760 million, down by 9.8% yoy.

The foreign exchange loss in the first three quarters was RMB180 million, and the profit in the same period of last year was RMB254 million. The foreign exchange loss in Q3 was RMB310 million (the profit in the same period of last year was RMB220 million). Excluding the impact of foreign exchange, the Company's actual profit in Q3 increased by 56.7% yoy, better than the market expectation, and the results in the first three quarters only decreased by 0.4%.

Significant Increase of Gross Margin and Well-established Leading Position

Thanks to reduction of SAM losses, improvement of capacity utilization, rising price of float glass and reduction of external sales, as well as improvement of product mix, the Company's gross margin in Q3 increased significantly by 4.1% yoy and 4.3% qoq, respectively, to 41.4%, which is the highest single quarter since 2019. At the same time, the Company strengthened expense control while maintained R&D input, with the sales expense rate of 6.9% (-0.1pct yoy), the administration expense ratio of 9.4% (-0.4pct yoy) and the R&D expense ratio of 4.1% (+0.5pct yoy). Due to the fact that the foreign exchange loss increased by RMB530 million yoy, the financial expense ratio was 5.4% (+8.7pct yoy).

During the first three quarters, the decline of the Company's domestic automotive glass revenue was better than the industry, reflecting the increase of the Company's domestic market share. The overseas epidemic has caused the competitors to suffer more severely, and the Company is expected to take advantage of the resumption of production to expand its overseas market share, and further strengthen its position as a global glass leader.

The upgrade path of the Company's products is quite clear. During the first three quarters, the share of high value-added products, such as insulation, head-up display and switchable glass, increased by approximately 2.6 ppts compared with the same period last year. As HUD glass and awning glass are leading the trend of automobile specification improvement, the product mix and market coverage of the intelligent glass application company will usher in a broader development space and promote the sustainable growth of subsequent result.

Overseas Business Bottomed Out and Interior Business Is About To Make Profit

The two major overseas businesses of Fuyao Glass have improved significantly. The US factory made a turnaround in Q3 with a profit of USD13.7 million, and its profitability is expected to increase further in Q4. The German SAM factory reduced its losses, with losses of EUR12.22 million in Q1, EUR13.95 million in Q2 and EUR5.7 million in Q3, respectively. The factory is expected to be close to break-even, when its losses fell sharply qoq in Q3. The matching value of single vehicle is 2-3 times that of automotive glass. We believe that SAM acquired by the Company in 2019 will have great performance flexibility in the future after one and a half years of integration.

BUY (Upgrade)

CMP HKD 37.35

(Closing price as at 19 November)

TARGET HKD 45 (+20.5%)

COMPANY DATA

O/S SHARES (MN) :	2509
MARKET CAP (HKD MN) :	18885
52 - WK HI/LO (HKD):	39.55/ 15.3

SHARE HOLDING PATTERN, %

Sanyi Development Limited	15.57
Heren Charitable Foundation	11.56

PRICE VS. HSI



Source: Aastock, Phillip Securities (HK) Research

KEY FINANCIALS

CNY mn	FY19	FY20	FY21E	FY22E
Net Sales	21104	19853	22682	26076
Net Profit	2898	2681	3637	4576
EPS, CNY	1.16	1.07	1.45	1.82
P/E, x	19.4	20.0	14.8	11.7
BVPS, CNY	8.52	8.83	9.65	10.61
P/BV, x	2.6	2.4	2.2	2.0
DPS (CNY)	0.75	0.63	0.85	1.18
Div. Yield (%)	3.3%	2.9%	4.0%	5.5%

Source: Company reports, Phillip Securities Est.

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Investment Thesis

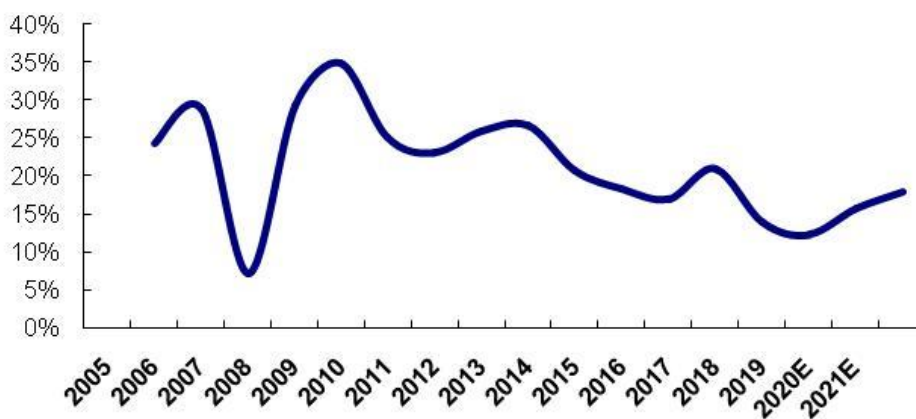
Overall, considering the steady leading position, continuous optimization of the product structure and a high dividend rate provide a greater margin of safety for the Company. We give the "Buy" rating, with target price to be HK\$45, equivalent to 36/26/21x P/E for 2020/2021/2022E. (Closing price as at 19 November)

Valuation trend



Source: Bloomberg, Phillip Securities Hong Kong Research

Fuyao's ROE trend



Source: Wind Phillip Securities Hong Kong Research

Risks

Demand for automobiles keeps sluggish; cost of raw materials increases; RMB appreciates

Catalyst

Success market development of overseas automobile market; rebound of domestic demand for automobile; depreciation of RMB

Financials

FYE DEC	FY17	FY18	FY19	FY20F	FY21F	FY22F
Valuation Ratios						
P/E (X), adj.	24.8	20.2	28.8	29.7	21.9	17.4
P/B (X)	4.1	4.1	3.9	3.6	3.3	3.0
Dividend Yield (%)	2.4%	3.5%	2.3%	2.0%	2.7%	3.7%
Per share data (RMB)						
EPS, (Basic)	1.25	1.64	1.16	1.07	1.45	1.82
EPS, (Diluted)	1.25	1.64	1.16	1.07	1.45	1.82
DPS	0.75	1.15	0.75	0.63	0.85	1.18
BVPS	7.58	8.05	8.52	8.83	9.65	10.61
Growth & Margins (%)						
Growth						
Revenue	12.6%	8.1%	4.3%	-5.9%	14.2%	15.0%
EBIT	-6.7%	37.7%	-33.8%	-4.8%	41.3%	25.1%
Net Income, adj.	0.2%	30.9%	-29.7%	-7.5%	35.6%	25.8%
Margins						
Gross margin	41.7%	41.5%	36.5%	37.4%	40.0%	41.1%
EBIT margin	19.8%	25.2%	16.0%	16.2%	20.0%	21.8%
Net Profit Margin	16.8%	20.4%	13.7%	13.5%	16.0%	17.5%
Key Ratios						
ROE	17.0%	21.0%	13.9%	12.3%	15.7%	18.0%
Income Statement (RMB mn)						
Revenue	18716	20225	21104	19853	22682	26076
Gross profit	7798	8397	7705	7431	9076	10728
EBIT	3705	5102	3379	3217	4545	5688
Profit before tax	3679	4962	3231	2980	4392	5535
Tax	531	855	333	301	747	935
Profit for the period	3148	4107	2898	2679	3646	4600
Minority interests	-1	-13	0	-2	9	24
Total capital share	2509	2509	2509	2509	2509	2509
Net profit	3148	4120	2898	2681	3637	4576

Source: PSR

(Closing price as at 19 November)

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 ± 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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