

Sanhua (002050 CH)

Scored New Orders, With Production Expansion

China | Automobile Components | Company Report

9 March 2021

Investment Summary

Gross Profit Margin Rose QoQ

According to the (unaudited) report for Q3 2020 disclosed by the Company, in the first three quarters, Sanhua recorded a revenue of RMB8,593 million, down 0.32% yoy, and a net profit attributable to shareholders of the listed company of RMB1,092 million, up 3.4% yoy. Specifically, the Company in Q3 reported a revenue of RMB3,275 million, up 17.40% yoy, and a net profit attributable to shareholders of the listed company of RMB449 million, up 23.51% yoy. The gross profit margin in the first three quarters was 28.69%, which was basically the same yoy. In Q3, the gross profit margin was 30.14%, a slight increase of 0.5 ppts yoy, and an increase of 1.14 ppts qoq. In Q3, the revenue of the Company's electric refrigeration and air conditioning parts business and auto parts business was approximately RMB2.63 billion and RMB650 million, respectively, an approximate increase of 10% and 50% yoy. The Company's outperformance in downstream sales volume and the improvement in product mix played a positive role in the recovery of profitability. The Company had good control on expenses. In the first three quarters, the period expense ratio was 15.09%, up 1.45 ppts yoy. Specifically, the financial expense ratio was 0.47%, up 0.83 ppts yoy, which was mainly affected by exchange gains and losses. The Company's net profit margin in Q3 reached 13.70%, up 0.68 ppts yoy.

The Company Continuously Obtains New Orders and New Energy Business Is Boosted Again

According to an announcement, Sanhua has recently won orders from several well-known customers:

- 1) The Company became the exclusive supplier of multiple thermal management valve products on the e-Platform of Fudi Technology under BYD, with cumulative sales of nearly RMB500 million in the five-year life cycle. The relevant models are expected to be mass-produced in 2021;
- 2) The Company was identified as the exclusive supplier of integrated thermal management components for GM's large-scale electric vehicle platform in North America, with sales expected to exceed RMB900 million;
- 3) The Company was identified as the exclusive supplier of products such as electronic expansion valves and integrated thermal management modules for the core platform for electric vehicles of SAIC Motor, with cumulative sales of more than RMB1 billion in the life cycle. The relevant models are expected to be mass-produced in 2022.

We believe that the Company's continuous receipt of orders from leading OEMs since 2017 has verified that its thermal management products and system capabilities have been continuously recognized. In the next 5-10 years, the Company will continue to focus on heat pump-related products for its new energy vehicle parts business. Compared with the PTC mode, the heat pump mode can reduce the power consumption by 2/3, which can greatly increase the cruising range. The Company has currently maintained a high capacity utilization rate and production-sales ratio. With the rapid development of the new energy vehicle market, the Company is expected to usher in a period of explosive growth of new orders.

Accumulate (Maintain)

CMP CNY 23.34

(Closing price as at 5 March)

TARGET CNY26.7 (+14.4%)

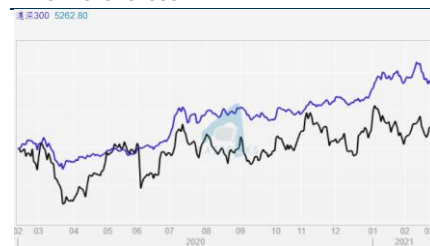
COMPANY DATA

O/S SHARES (MN) :	3592
MARKET CAP (CNY MN) :	83828
52 - WK HI/LO (CNY):	28.15/ 15.11

SHARE HOLDING PATTERN, %

Mr Zhangs'	46
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PRICE VS. SHSZ300



Source: Phillip Securities (HK) Research

KEY FINANCIALS

CNY mn	FY18	FY20	FY21E	FY22E
Net Sales	11288	11986	15134	17091
Net Profit	1421	1530	2067	2505
EPS, CNY	0.51	0.43	0.58	0.70
P/E, x	45.4	54.8	40.6	33.5
BVPS, CNY	3.36	2.84	3.19	3.58
P/BV, x	6.9	8.2	7.3	6.5
DPS (CNY)	0.15	0.17	0.23	0.30
Div. Yield (%)	0.6%	0.7%	1.0%	1.3%

Source: Company reports, Phillip Securities Est.

Research Analyst

Zhangjing (+ 86 21-51699400-103)

zhangjing@phillip.com.cn

Raising Funds for Production Expansion Facilitates the Development

In order to expand the commercial refrigeration market, the Company plans to issue convertible bonds to raise funds amounting to RMB3 billion, which will be used to increase commercial refrigeration production capacity. It includes a construction project with an annual output of 65 million sets of intelligent control components for commercial refrigeration and air conditioning, and a technical renovation project with an annual output of 50.5 million sets of high-efficiency and energy-saving refrigeration and air-conditioning control components. The construction period is six years and four years, respectively. The new expansion project will help the Company expand the product line, optimize the product mix and increase the revenue and profitability in the future. Commercial refrigeration products have a higher gross profit margin. If domestic substitution can be achieved, the Company's competitiveness will be consolidated.

Investment Thesis

Sanhua is the leading company of refrigeration parts and components with obvious technical advantages in its products. The thermal management of new energy vehicles, dishwashers and cold-chain logistics are all promising business areas in line with the general direction of social development in the future. We expect that the Company's home appliance business will benefit from the market share increase year by year. There is a broad market for the thermal management of new energy vehicles in the future. Under a clear pattern of dual-driven growth, the Company is entering a period of realizing high growth of result.

As for valuation, we expected diluted EPS of the Company to RMB0.43/0.58/0.70 of 2020/2021/2022. And we accordingly gave the target price to RMB26.7, respectively 63/46/38x P/E for 2020/2021/2022. "Accumulate" rating. (Closing price as at 5 March)

Risk

- Progress of new production line is below expectations
- Electric vehicle sales fall short of expectations
- Macroeconomic downturn affects product demand
- Sharply rising raw material prices or sharply falling product prices

Financials

FYE DEC	FY18	FY19	FY20F	FY21F	FY22F
Valuation Ratios					
P/E (X), adj.	38.3	45.4	54.8	40.6	33.5
P/B (X)	5.8	6.9	8.2	7.3	6.5
Dividend Yield (%)	1.1%	0.6%	0.7%	1.0%	1.3%
Per share data (RMB)					
EPS, (Basic)	0.61	0.51	0.43	0.58	0.70
EPS, (Diluted)	0.61	0.51	0.43	0.58	0.70
DPS	0.25	0.15	0.17	0.23	0.30
BVPS	4.04	3.36	2.84	3.19	3.58
Growth & Margins (%)					
Growth					
Revenue	13.1%	4.2%	6.2%	26.3%	12.9%
EBIT	-6.5%	11.1%	3.1%	38.6%	20.9%
Net Income, adj.	4.5%	10.0%	7.7%	35.0%	21.2%
Margins					
Gross margin	28.6%	29.6%	28.3%	29.4%	30.5%
EBIT margin	13.8%	14.7%	14.3%	15.7%	16.8%
Net Profit Margin	11.9%	12.6%	12.8%	13.7%	14.7%
Key Ratios					
ROE	15.7%	13.9%	13.7%	19.1%	20.6%
Income Statement (RMB mn)					
Revenue	10836	11288	11986	15134	17091
Gross profit	3098	3341	3397	4454	5213
EBIT	1494	1660	1712	2372	2867
Profit before tax	1539	1663	1737	2351	2852
Tax	228	229	195	264	321
Profit for the period	1311	1434	1541	2087	2531
Minority interests	19	13	11	20	26
Total capital share	2120	2765	3592	3592	3592
Net profit	1292	1421	1530	2067	2505

Source: PSR

(Closing price as at 5 March)

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

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

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

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

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

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

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

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

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

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

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

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