

Weichai Power (000338 CH)

Impressive 1Q23 earnings; U/G to BUY; More catalysts ahead

Weichai's 1Q23 net profit growth of 68% YoY is above our expectation. We believe the impressive earnings growth was driven by the strong operating leverage of the HDT engine segment. We are turning more positive on Weichai's recovery story, with new catalysts coming from: (1) the recent sharp decline in LNG price (down ~40% since Dec) that will boost the sales of LNG trucks/engines, where Weichai has strong presence on; (2) the easing supply chain pressure that will help KION achieve strong-than-expected margin recovery. All these, together with the continuous growth of engines for agricultural machinery and HDT through rising penetration in LOVOL and **Sinotruk (3808 HK)**, prompted us to revise up our earnings forecast in 2023E/24E by 30%/28%. Our SOTP-based TPs for Weichai A/H are revised up to RMB13.8/HK\$15.8. Given that the H/A discount (currently 11%) has been narrowed and is close to the historical average of 12%, we **upgrade Weichai-A to BUY** from Hold and maintain **BUY** on Weichai-H.

- 1Q23 results highlights.** Weichai's revenue of RMB53.4bn in 1Q23 represented 30%/18% YoY growth, respectively, before/after restatement of 1Q22 figures (Note: LOVOL was a JV in 1Q22 as the consolidation took place in Jun 2022). We believe the revenue growth in 1Q23 was driven by the strong HDT engine sales volume and operating leverage. Gross margin was largely stable at 18.7% in 1Q23. With both SG&A and R&D expense ratio reduced in 1Q23, net profit surged 77%/68% YoY (before/after restatement) to RMB1.86bn. Based on our calculation, the pretax profit (excluding KION) surged ~1.6x YoY in 1Q23. Operating cash flow in 1Q23 substantially improved to -RMB471mn (1Q22: -RMB3.2bn).
- Weichai's engine sales outpaced industry in 1Q23.** According to CICEIA, Weichai's multi-cylinder sales grew ~6% YoY to 183k units in 1Q23 (vs the industry average of a decline of ~3%), with a market share of ~16%.
- Decline in LNG price positive to Weichai.** LNG price in late Apr has declined 40%+ from the peak in Dec 2022. We believe it will potentially boost the sales of LNG trucks given the lower operating cost to truck owners. We expect Weichai to be a key beneficiary as we estimate Weichai has >40% market share in HDT gas engine.
- Higher earnings guidance for KION Group.** KION (45.2% owned by Weichai) reported net income of EUR73.5mn in 1Q23 (-8% YoY), largely due to higher net finance expense. In the 1Q23 report, KION revised up the full year adjusted EBIT target to EUR615mn from EUR500mn due to improving supply chains.

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	203,548	175,158	209,751	226,204	238,954
YoY growth (%)	3.1	(13.9)	19.7	7.8	5.6
Adjusted net profit (RMB mn)	9,254.6	4,905.5	7,193.8	8,265.2	9,100.7
EPS (Reported) (RMB)	1.06	0.56	0.82	0.95	1.04
YoY growth (%)	(8.6)	(47.0)	46.6	14.9	10.1
Consensus EPS (RMB)	na	na	0.78	0.98	1.08
P/E (x)	17.4	21.8	14.0	12.2	11.0
P/B (x)	2.3	1.5	1.3	1.2	1.1
Yield (%)	1.9	2.1	2.5	2.9	3.2
Net gearing (%)	(61.0)	(62.3)	(72.8)	(85.8)	(85.8)

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Up)

Target Price RMB13.80

(Previous TP) RMB11.40

Up/Downside 19.8%

Current Price RMB11.52

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Stock Data

Mkt Cap (RMB mn)	100,529.9
Avg 3 mths t/o (RMB mn)	565.0
52w High/Low (RMB)	12.98/9.08
Total Issued Shares (mn)	8726.6

Source: FactSet

Shareholding Structure

Weichai Holdings Group	16.3%
Weifang Investment Group	3.4%

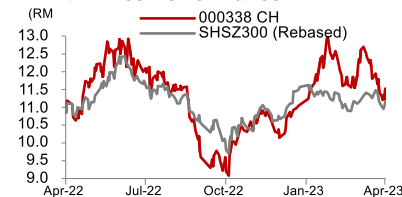
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-5.7%	-6.3%
3-mth	4.1%	8.0%
6-mth	25.2%	10.1%

Source: FactSet

12-month Price Performance



Source: FactSet

Related reports:

China Construction Machinery & HDT Sector – 2023 outlook: Difficulties mastered are opportunities won – 7 Dec 2022 ([link](#))

Weichai Power-H (2338 HK, BUY) – Valuation close to the trough – 31 Oct 2022 ([link](#))

Weichai Power-A (000338 CH, HOLD) – Expect further earnings cut by the Street; Prefer Weichai-H for large valuation discount – 31 Oct 2022 ([link](#))

Figure 1: Weichai's quarterly results

(RMB mn)	1Q22	1Q23	Chg (YoY)	2Q21	2Q22	Chg (YoY)	3Q21	3Q22	Chg (YoY)	4Q21	4Q22	Chg (YoY)
Revenue	41,104	53,434	30%	60,917	45,636	-25%	40,041	43,783	9%	37,119	44,634	20%
Cost of sales	-33,445	-43,442	30%	-49,648	-37,924	-24%	-31,888	-37,080	16%	-29,482	-35,561	21%
Gross profit	7,659	9,992	30%	11,269	7,712	-32%	8,153	6,704	-18%	7,637	9,073	19%
Other income	168	126	-25%	243	202	-17%	133	254	92%	136	498	268%
Other gains and losses	139	116	-16%	106	505	376%	170	599	252%	339	224	-34%
S&D expenses	-2,553	-2,866	12%	-2,905	-2,459	-15%	-2,630	-2,799	6%	-1,959	-2,850	45%
Administrative expenses	-1,878	-2,295	22%	-1,983	-2,000	1%	-1,897	-2,007	6%	-1,949	-2,207	13%
R&D expenses	-1,828	-1,833	0%	-1,839	-1,860	1%	-1,471	-1,827	24%	-1,850	-2,217	20%
Taxes and surcharges	-82	-126	54%	-245	-139	-43%	-78	-100	27%	-204	-159	-22%
Impairment loss of assets	-220	-337	53%	-21	-420	1888%	-152	-277	83%	-486	-370	-24%
EBIT	1,405	2,777	98%	4,624	1,539	-67%	2,228	549	-75%	1,664	1,990	20%
Other expenses	-39	-41	6%	-24	-20	-16%	-12	-24	103%	-81	-79	-3%
Net finance cost	156	-52	n/a	97	371	281%	194	67	-66%	61	316	417%
Share of profit of JV and associates	58	-33	n/a	95	-51	n/a	43	-59	n/a	-15	-92	529%
Pretax profit	1,579	2,651	68%	4,793	1,839	-62%	2,453	533	-78%	1,629	2,135	31%
Income tax	-270	-405	50%	-905	-196	-78%	-517	252	n/a	-258	-189	-27%
After tax profit	1,309	2,245	72%	3,888	1,643	-58%	1,936	784	-59%	1,371	1,947	42%
MI	-258	-389	51%	-800	-307	-62%	-467	141	n/a	-17	-353	1995%
Net profit	1,051	1,856	77%	3,088	1,335	-57%	1,469	925	-37%	1,354	1,594	18%
Key ratios			Chg (ppt)			Chg (ppt)			Chg (ppt)			Chg (ppt)
Gross margin	18.6%	18.7%	0.1	18.5%	16.9%	-1.6	20.4%	15.3%	-5.1	20.6%	20.3%	-0.2
S&D expense ratio	6.2%	5.4%	-0.8	4.8%	5.4%	0.6	6.6%	6.4%	-0.2	5.3%	6.4%	1.1
Administrative expense ratio	4.6%	4.3%	-0.3	3.3%	4.4%	1.1	4.7%	4.6%	-0.2	5.3%	4.9%	-0.3
R&D expense ratio	4.4%	3.4%	-1.0	3.0%	4.1%	1.1	3.7%	4.2%	0.5	5.0%	5.0%	0.0
Effective tax rate	17.1%	15.3%	-1.8	18.9%	10.7%	-8.2	21.1%	-47.3%	-68.4	15.9%	8.8%	-7.0

Source: Company data, CMBIGM

Note: Figures for 1Q22 are before restatement

Figure 2: KION's latest guidance for 2023E

(EUR mn)	2020	2021	2022	2023E guidance	
				Old	New
Order intake	9,443	12,482	11,708	-	-
Growth (YoY)	4%	32%	-6%	-	-
Revenue	8,342	10,294	11,136	11,000	11,200
Growth (YoY)	-5%	23%	8%	-1%	1%
Adjusted EBIT	547	842	292	550	615
Growth (YoY)	-36%	54%	-65%	88%	111%
Adjusted EBIT margin	6.6%	8.2%	2.6%	5.0%	5.5%
Net income	211	568	106	-	-
Growth (YoY)	-53%	169%	-81%	-	-

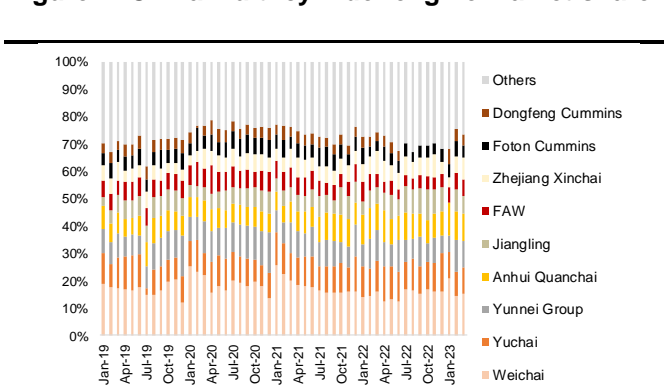
Source: Company data, CMBIGM

Figure 3: KION's quarterly financials

(EUR mn)	1Q22	2Q22	3Q22	4Q22	1Q23
Order intake	2,900	3,755	2,517	2,536	2,444
Growth (YoY)	10%	15%	-19%	-27%	-16%
Revenue	2,734	2,802	2,706	2,893	2,781
Growth (YoY)	15%	8%	5%	5%	2%
Adjusted EBIT	170	141	-101	82	156
Growth (YoY)	-21%	-43%	n/a	-46%	-8%
Adjusted EBIT margin	6.2%	5.0%	-3.7%	2.8%	5.6%
Net income	80	80	-93	39	74
Growth (YoY)	-41%	-48%	n/a	-72%	-8%

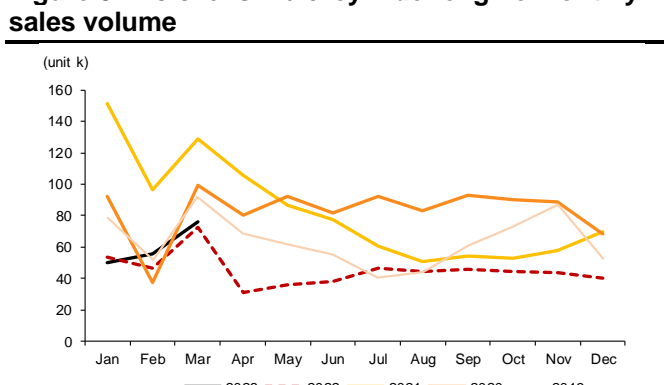
Source: Company data, CMBIGM

Figure 4: China multi-cylinder engine market share



Source: CICEIA, CMBIGM

Figure 5: Weichai's multi-cylinder engine monthly sales volume



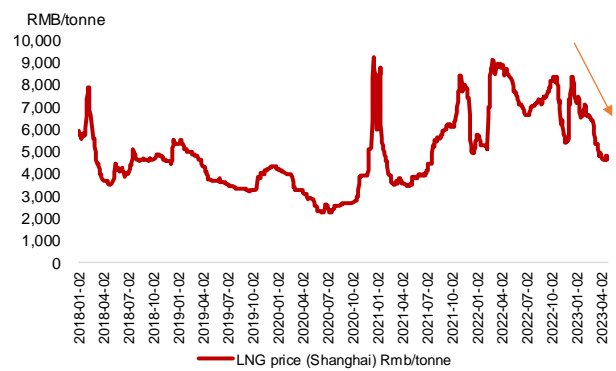
Source: CICEIA, CMBIGM

Figure 6: Shandong diesel price



Source: Wind, CMBIGM

Figure 7: Shanghai LNG price



Source: Wind, CMBIGM

Figure 8: Change in key assumptions for Weichai

Change in key assumptions	2023E			2024E			2025E		
	Old	New	Change	Old	New	Change	Old	New	Change
Sales volume (unit)									
Engine total	809,552	844,481	4.3%	889,728	941,134	5.8%	-	1,005,504	-
HDT (Shaanxi Heavy-duty Motor)	72,900	104,000	42.7%	74,358	111,280	49.7%	-	116,844	-
Gear box (Shaanxi Fast Gear Company)	605,325	737,500	21.8%	617,432	781,750	26.6%	-	813,020	-
(RMB mn)									
Revenue									
Diesel engines	49,383	57,763	17.0%	55,163	64,374	16.7%	-	68,776	-
Automobiles and major components	37,302	58,905	57.9%	38,048	62,512	64.3%	-	65,090	-
Forklift trucks & supply chain solution	85,339	82,171	-3.7%	90,459	87,101	-3.7%	-	92,327	-
Agricultural machinery	20,503	19,860	-3.1%	22,553	21,846	-3.1%	-	22,939	-
Intersegment sales	-8,601	-8,948	4.0%	-9,184	-9,629	4.9%	-	-10,179	-
Total revenue	183,926	209,751	14.0%	197,040	226,204	14.8%	-	238,954	-
Segment profit									
Diesel engines	3,704	4,794	29.4%	4,413	5,472	24.0%	-	5,846	-
Automobiles and major components	149	648	334.3%	304	813	167.0%	-	911	-
Forklift trucks & supply chain solution	1,536	1,643	7.0%	1,809	2,352	30.0%	-	2,677	-
Agricultural machinery	902	874	-3.1%	1,015	983	-3.1%	-	1,032	-
Intersegment sales	-86	-89	4.0%	-92	-96	4.9%	-	-102	-
Total segment profit	6,205	7,870	26.8%	7,450	9,523	27.8%	-	10,365	-
Segment margin			<i>Chg (ppt)</i>			<i>Chg (ppt)</i>			<i>Chg (ppt)</i>
Diesel engines	7.5%	8.3%	0.8	8.0%	8.5%	0.5	-	8.5%	-
Automobiles and major components	0.4%	1.1%	0.7	0.8%	1.3%	0.5	-	1.4%	-
Forklift trucks & supply chain solution	1.8%	2.0%	0.2	2.0%	2.7%	0.7	-	2.9%	-
Agricultural machinery	4.4%	4.4%	0.0	4.5%	4.5%	0.0	-	4.5%	-
Average	3.4%	3.8%	0.4	3.8%	4.2%	0.4	-	4.3%	-
Net profit	5,535	7,194	30.0%	6,453	8,265	28.1%	-	9,101	-

Source: Company data, CMBIGM estimates

Figure 9: SOTP valuation (new)

SOTP valuation	Valuation methodology	Target multiple (x)	EBITDA 2023E (RMB mn)	Estimated EV (RMB mn)	Net cash / (Net debt)	Equity value (RMB mn)	Equity value breakdown
Weichai core business	EV/EBITDA	7.0	8,822	61,756	38,674	100,429	83.7%
KION Group	Proportionate market value	-	-	-	-	17,136	14.3%
Ballard Power Systems	Proportionate market value	-	-	-	-	1,799	1.5%
Ceres Power	Proportionate market value	-	-	-	-	1,142	1.0%
Share of JV/associates	P/B	1.2	-	-	-	6,409	5.3%
Minority interest in core business						-6,899	-5.7%
Total NAV						120,017	100.0%
NAV per share (RMB)						13.8	
NAV per share (HK\$)						15.8	

Source: Company data, CMBIGM estimates

Note 1: Weichai owns 45.2% interest in KION, 20% interest in Ballard Power and 20% interest in Ceres Power.

Note 2: Share of JV / associates exclude Ballard Power and Ceres Power

Figure 10: SOTP valuation (previous)

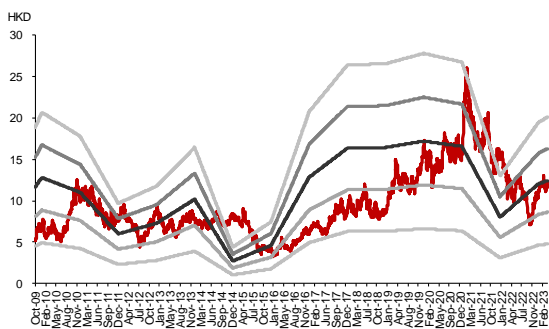
SOTP valuation	Valuation methodology	Target multiple (x)	EBITDA 2023E (RMB mn)	Estimated EV (RMB mn)	Net cash / (Net debt)	Equity value (RMB mn)	Equity value breakdown
Weichai core business	EV/EBITDA	6.0	7,233	43,397	42,049	85,447	85.7%
KION Group	Proportionate market value	-	-	-	-	12,775	12.8%
Ballard Power Systems	Proportionate market value	-	-	-	-	2,604	2.6%
Ceres Power	Proportionate market value	-	-	-	-	1,280	1.3%
Share of JV/associates	P/B	1.0	-	-	-	3,518	3.5%
Minority interest in core business						-5,913	-5.9%
Total NAV						99,710	100.0%
NAV per share (RMB)						11.4	
NAV per share (HK\$)						12.6	

Source: Company data, CMBIGM estimates

Note 1: Weichai owns 45.2% interest in KION, 20% interest in Ballard Power and 20% interest in Ceres Power.

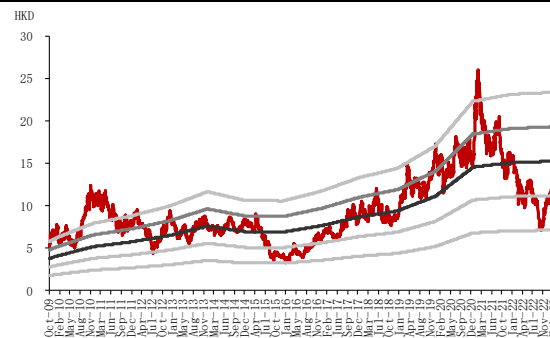
Note 2: Share of JV / associates exclude Ballard Power and Ceres Power

Figure 11: Weichai Power-H P/E band



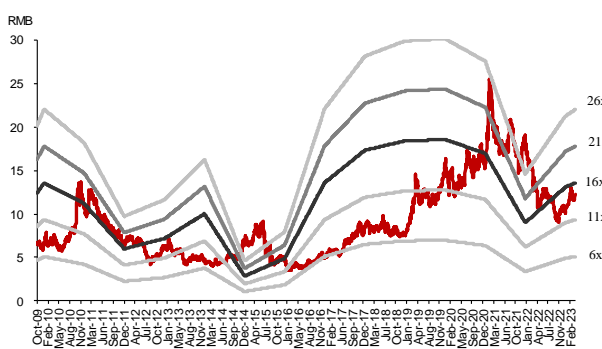
Source: Bloomberg, Company data, CMBIGM estimates

Figure 12: Weichai Power-H P/B band



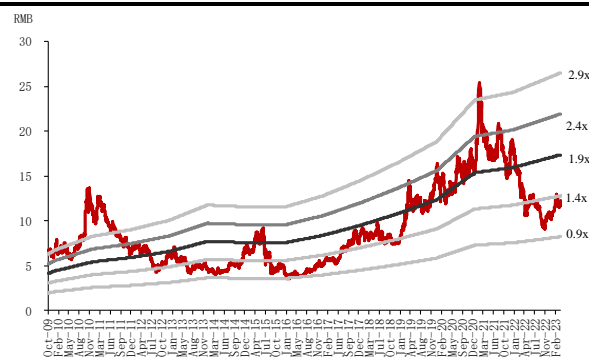
Source: Bloomberg, Company data, CMBIGM estimates

Figure 13: Weichai Power-A P/E band



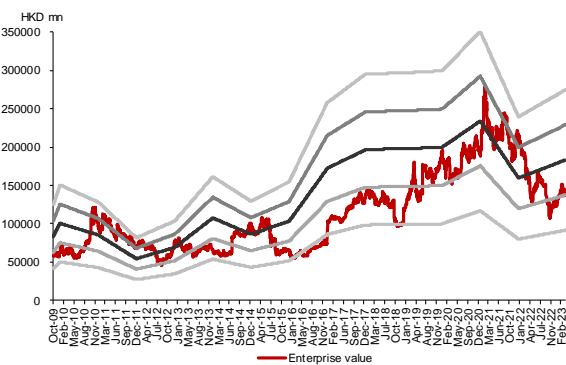
Source: Bloomberg, Company data, CMBIGM estimates

Figure 14: Weichai Power-A P/B band



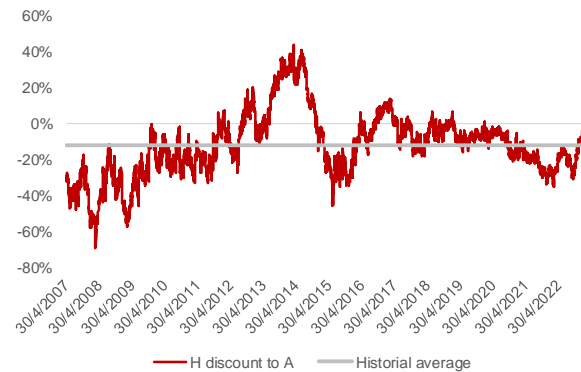
Source: Bloomberg, Company data, CMBIGM estimates

Figure 15: Weichai Power EV/EBITDA band



Source: Bloomberg, Company data, CMBIGM estimates

Figure 16: Weichai Power H discount to A



Source: Bloomberg, CMBIGM

Risk factors: (1) Weakness in engine demand; (2) increase in component cost; and (3) new business growth below expectations

Financial Summary

INCOME STATEMENT	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Revenue	197,491	203,548	175,158	209,751	226,204	238,954
Cost of goods sold	(159,353)	(163,947)	(144,011)	(170,318)	(183,225)	(193,553)
Gross profit	38,138	39,601	31,147	39,433	42,979	45,401
Operating expenses	(25,289)	(26,038)	(25,664)	(30,051)	(31,927)	(33,483)
Operating profit	12,850	13,563	5,482	9,382	11,052	11,918
Share of (losses)/profits of associates/JV	253	187	(144)	188	191	177
EBITDA	21,708	24,160	16,630	20,661	22,953	24,451
Depreciation	8,858	10,597	11,148	11,279	11,902	12,533
Interest income	1,278	1,724	2,359	2,026	2,220	2,544
Interest expense	(1,557)	(1,274)	(1,450)	(1,721)	(1,737)	(1,741)
Net Interest income/(expense)	(279)	450	909	304	483	803
Other income/expense	(142)	(145)	(162)	(252)	(271)	(287)
Pre-tax profit	12,682	14,055	6,086	9,623	11,454	12,612
Income tax	(1,407)	(2,493)	(403)	(1,540)	(2,062)	(2,270)
Minority interest	(2,068)	(2,307)	(778)	(889)	(1,127)	(1,241)
Adjusted net profit	9,207	9,255	4,906	7,194	8,265	9,101
BALANCE SHEET	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Current assets	152,515	160,638	168,484	187,549	196,321	218,434
Cash & equivalents	62,216	75,043	70,842	73,845	84,705	97,016
Account receivables	15,422	18,191	21,419	26,853	27,684	29,927
Inventories	31,226	31,585	33,374	44,086	41,252	48,896
Prepayment	1,095	1,570	1,473	1,388	1,303	1,218
Other current assets	42,556	34,249	41,378	41,378	41,378	41,378
Non-current assets	118,235	116,406	125,182	122,468	117,634	112,162
PP&E	31,720	33,188	37,892	36,173	32,349	27,865
Investment in JVs & assos	4,944	6,713	5,341	5,422	5,504	5,580
Intangibles	23,826	20,908	22,760	21,684	20,592	19,527
Goodwill	24,666	22,847	24,019	24,019	24,019	24,019
Other non-current assets	33,079	32,750	35,171	35,171	35,171	35,171
Total assets	270,750	277,044	293,666	310,017	313,955	330,596
Current liabilities	123,713	115,382	114,440	121,816	119,210	119,210
Short-term borrowings	17,006	12,982	13,782	14,582	14,682	14,682
Account payables	45,450	39,596	37,854	44,430	41,724	41,724
Other current liabilities	61,257	62,803	62,803	62,803	62,803	62,803
Non-current liabilities	66,604	58,700	58,200	58,200	58,200	58,200
Long-term borrowings	20,729	18,839	18,339	18,339	18,339	18,339
Other non-current liabilities	45,876	39,861	39,861	39,861	39,861	39,861
Total liabilities	190,317	174,083	172,640	180,016	177,411	177,411
Total shareholders equity	51,202	70,907	75,614	82,028	89,094	89,094
Minority interest	29,231	32,055	34,293	36,886	39,786	39,786
Total equity and liabilities	270,750	277,044	282,548	298,930	306,291	306,291

CASH FLOW	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	12,682	14,055	6,086	9,623	11,454	12,612
Depreciation & amortization	8,787	10,537	11,065	11,194	11,817	12,448
Tax paid	(1,407)	(2,493)	(403)	(1,540)	(2,062)	(2,270)
Change in working capital	1,114	(8,767)	(20,324)	(6,476)	(1,034)	(795)
Others	1,753	1,325	1,227	1,618	1,631	1,648
Net cash from operations	22,928	14,658	(2,350)	14,420	21,806	23,643
Investing						
Capital expenditure	(5,992)	(3,610)	(5,242)	(8,400)	(6,900)	(6,900)
Acquisition of subsidiaries/ investments	(1,475)	(3,578)	(309)	0	0	0
Others	(1,950)	1,779	(2,995)	107	109	101
Net cash from investing	(9,417)	(5,409)	(8,545)	(8,293)	(6,791)	(6,799)
Financing						
Dividend paid	(3,459)	(4,715)	(3,930)	(2,203)	(2,518)	(2,893)
Net borrowings	1,052	(5,913)	12,842	800	100	100
Proceeds from share issues	0	14,050	1,676	0	0	0
Others	(579)	(298)	(5,736)	(1,721)	(1,737)	(1,741)
Net cash from financing	(2,986)	3,123	4,852	(3,124)	(4,155)	(4,533)
Net change in cash						
Cash at the beginning of the year	48,818	62,216	75,043	70,842	73,845	84,705
Exchange difference	2,873	455	1,841	0	0	0
Cash at the end of the year	62,216	75,043	70,842	73,845	84,705	97,016
GROWTH	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Revenue	13.3%	3.1%	(13.9%)	19.7%	7.8%	5.6%
Gross profit	0.3%	3.8%	(21.3%)	26.6%	9.0%	5.6%
Operating profit	(10.9%)	5.5%	(59.6%)	71.1%	17.8%	7.8%
EBITDA	(3.5%)	11.3%	(31.2%)	24.2%	11.1%	6.5%
Adj. net profit	1.1%	0.5%	(47.0%)	46.6%	14.9%	10.1%
PROFITABILITY	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Gross profit margin	19.3%	19.5%	17.8%	18.8%	19.0%	19.0%
Operating margin	6.5%	6.7%	3.1%	4.5%	4.9%	5.0%
EBITDA margin	11.0%	11.9%	9.5%	9.9%	10.1%	10.2%
Adj. net profit margin	4.7%	4.5%	2.8%	3.4%	3.7%	3.8%
GEARING/LIQUIDITY/ACTIVITIES	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Net debt to equity (x)	(0.5)	(0.6)	(0.6)	(0.7)	(0.9)	(0.9)
Current ratio (x)	1.2	1.4	1.5	1.5	1.6	1.8
Receivable turnover days	27.5	30.1	41.3	42.0	44.0	44.0
Inventory turnover days	64.1	69.9	82.3	83.0	85.0	85.0
Payable turnover days	94.1	94.7	107.9	108.0	107.0	107.0
VALUATION	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
P/E	12.8	17.4	21.8	14.0	12.2	11.0
P/B	2.3	2.3	1.5	1.3	1.2	1.1
Div yield (%)	2.7	1.9	2.1	2.5	2.9	3.2

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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