

Huami Corp (HMI, BUY, TP: \$20.10)

BUY

HOLD

SELL

Target Price: \$20.10 Current Price: \$14.00

52-Week High \$17.61
52-Week Low \$7.27
EV (MM) \$675
Market Cap (MM) \$858
Shares Outstanding (MM) 245
Average Daily Trading Volume (MM) 0.5

Priced as of close on 13 March 2020.

Source: FactSet

Price Performance



Source: FactSet

China Renaissance vs Consensus (% diff)

	2020E	2021E
Rev (MM) (RMB)	7,045 (+11%)	7,967 (+9%)
EPS (RMB)	10.37 (+13.04%)	10.77 (+25.96%)

Note: Consensus estimates displayed, sourced from Bloomberg. Positive % diff = CR est. above consensus; negative = CR est. below consensus.

Another beat; Self-branded momentum continues

- Momentum for self-branded products continues.
- Xiaomi and Huami relationship seems intact.
- Maintain BUY, adjust TP to US\$20.10.

Huami delivered solid 4Q19 results. Revenue reached RMB2,111mn, up 72% YoY, missing/beat our estimates/consensus by 5%/3%, respectively. Adjusted net income reached RMB213.8mn, up 46% YoY, beating our estimates/consensus by 6%/1%. The GM was down to 23.8%, compared with 25.2% in 4Q18, due to the lower GM of Xiaomi products. Total Opex reached 285.5mn in 4Q19, up 61% YoY, due to higher selling & marketing and R&D expenses. Management guided 1Q20 revenue of RMB980mn-RMB1,010mn, up 22.6%-26.3% YoY.

Momentum for self-branded products continues amid risks of COVID-19 impact.

Total product shipments reached 42.3mn in 2019. We estimate 34.5mn unit shipments for Xiaomi (1810 HK, BUY, TP: HK \$15.07) products, 3.99mn units for self-branded products, and 3.8mn units for other products in 2019E. We expect Huami's self-branded wearable devices to achieve shipment volume of 6.42mn/7.71mn units in 2020/21E, increasing by 61%/20% YoY, respectively, driven by its international expansion and enriched product portfolio. However, we expect that if COVID-19 continues to spread globally, it will impact the product demand in overseas markets, especially for self-branded products whose overseas shipments represent 51.6% of the total.

Xiaomi relationship seems intact. Huami management reiterated that its partnership with Xiaomi continues for future Mi band design and manufacture. Management also mentioned being involved in the R&D phase for Mi Band 5, which is expected to be introduced in 2Q20. Management believes the company's cutting-edge algorithm accuracy and hardware design capacity will differentiate it from new smart watch/band products launched by Xiaomi in Nov 2019.

Maintain BUY, adjust TP to US\$20.10. Our new TP of US\$20.10 (down from US\$20.70) is based on an unchanged 2020E target P/E of 12x and revised 2020E diluted EPADS of US\$1.67 (down from US\$1.73). **Risks include:** COVID-19 outbreak persists, changes to the agreement with Xiaomi, and slow overseas expansion.

Research Team

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Summary Financial Data

Fiscal year-end: Dec	2018A	2019A	2020E	2021E	2022E
Revenue (MM) (RMB)	3,645	5,812	7,787	8,679	10,051
Operating Income (MM) (RMB)	366	607	753	875	1,022
Net Income (MM) (RMB)	475	630	750	868	1,011
EPS (RMB)	7.59	9.81	11.72	13.57	15.80
P/E	13x	10x	8x	7x	6x

EPS: Refers to non-GAAP diluted EPADS (1 ADS represents 4 ordinary shares).

Net Income (MM): Refers to non-GAAP net income

Source: China Renaissance Securities (Hong Kong) Limited

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Exhibit 1 - Key assumption changes

Earning summary (RMBmn)	Previous		Diff%-E	4Q19C	Diff%-C	4Q18	YoY%	3Q19	QoQ%	1Q20E
	4Q19	4Q19E								
Revenue	2,111	2,231	-5%	2,054	3%	1,225	72%	1,863	13%	1,137
Cost of Revenue	1,608	1,648	-2%	1,525	5%	916	76%	1,393	15%	831
Gross Profit	503	583	-14%	529	-5%	309	63%	470	7%	307
Gross margin	23.8%	26.1%	-230bps	25.8%	-192bps	25.2%	-140bps	25.2%	-140bps	27.0%
Selling and marketing expenses	63	78	-20%			29	118%	57	11%	45
General and admin expenses	83	112	-26%			64	29%	70	19%	57
Research and development expenses	140	167	-16%			85	65%	125	13%	85
Operating expense	285	357	-20%			178	61%	251	14%	188
Operating profit (loss)	218	226	-4%	224	-3%	131	66%	219	-1%	119
Operating margin	10.3%	10.1%	18bps	10.9%	-60bps	10.7%	-41bps	11.8%	-146bps	10.5%
Profit (loss) before income tax /PBT	237	221	7%	227		139	70%	228	4%	135
Income tax	27	27	1%	27		12	122%	28	-1%	15
Net income (loss)	206	194	6%	200	3%	125	65%	203	1%	119
Net margin	9.8%	8.7%	107bps	9.7%	4bps	10.2%	-45bps	10.9%	-115bps	10.5%
Non-GAAP net income	214	201	6%	212	1%	146	46%	210	2%	125
Non-GAAP net margin	10.1%	9.0%	111bps	10.3%	-17bps	12.0%	-184bps	11.3%	-114bps	11.0%

Source: Company data, CRS HK estimates. Note: USD/RMB=7.01.

Exhibit 2 - Key assumption changes

	OLD			NEW			CHANGE		
	2020E	2021E	2022E	2020E	2021E	2022E	2020E	2021E	2022E
Shipments (mnpcs)									
Xiaomi product shipments	38	39	40	38	39	39	-0.5%	-0.5%	-0.5%
Self-branded wearable products shipments	7.8	9.4	11.3	6.4	7.7	9.3	-18.1%	-18.1%	-18.1%
ASP (RMB)									
Xiaomi product ASP	123	125	134	125	127	135	1.8%	1.3%	1.1%
Self-branded wearable products ASP	439	456	479	421	437	459	-4.1%	-4.1%	-4.1%
Revenues (RMBmn)									
Xiaomi product revenues	4,678	4,862	5,299	4,737	4,899	5,329	1.3%	0.8%	0.6%
Self-branded products revenues	3,439	4,292	5,408	2,702	3,372	4,249	-21.4%	-21.4%	-21.4%
Data-based service revenues	48	61	74	49	64	78	3.3%	3.9%	4.4%
Total revenues	8,165	9,215	10,781	7,787	8,679	10,051	-4.6%	-5.8%	-6.8%
Gross margin									
Xiaomi products GM	23.2%	23.3%	23.3%	22.6%	23.3%	23.4%	-61bps	0bps	10bps
Self-branded products GM	31.6%	30.4%	30.4%	31.6%	30.3%	31.9%	-8bps	-13bps	147bps
Data-based service GM	100%	100%	100%	100%	100%	100%	0bps	0bps	0bps
Blended Gross Margin	27%	27%	27%	26%	27%	27%	-102bps	-55bps	-74bps
Other Financial Data (RMBmn)									
Total Gross Profit	2,220	2,500	2,955	2,038	2,307	2,680	-8.2%	-7.7%	-9.3%
Non-GAAP net income	781	882	1,061	750	868	1,011	-4.0%	-1.5%	-4.7%
Non-GAAP Diluted EPADS (RMB)	12.09	13.65	16.42	11.72	13.57	15.80	-3.1%	-0.6%	-3.8%
Non-GAAP Diluted EPADS (USD)	1.73	1.95	2.35	1.67	1.94	2.26	-3.1%	-0.6%	-3.8%

Source: Company data, CRS HK estimates. Note: USD/RMB=7.00.

Estimate revisions

We revise our forecasts for Xiaomi product shipments by -0.5%/-0.5%/-0.5% in 2020/21/22E due to slightly lower-than-expected Xiaomi shipments delivered in 4Q19.

We revise our self-branded wearables shipment forecasts by -18.1%/-18.1%/-18.1% in 2020/21/22E as the self-branded products shipments reached 3.99mn in 2019, lower than our previous estimate of 4.87mn.

We revise Xiaomi product and self-branded product ASP by 1.8%/1.3%/1.1% and -4.1%/-4.1%/-4.1%, respectively, mainly as a result of: 1) Xiaomi's ASP delivered in 4Q19 being higher than our expectation, while that of self-branded products was lower than our expectation; 2) we have separated the "others" segment from Xiaomi wearables under Xiaomi revenue from this earnings result onwards, due to the increased shipment of "other products", according to our channel checks, and this has caused a slight revision in the ASP delivered for both products.

Our revisions for both Xiaomi and self-branded products are mainly as a result of the difference between reported 4Q19 numbers and our previous estimates.

We revise our overall revenue forecasts by -4.6%/-5.8%/-6.8%, non-GAAP net income forecasts by -4.0%/-1.5%/-4.7% and non-GAAP diluted EPADS (RMB) forecasts by -3.1%/-0.6%/-3.8%.

Valuation

We cut our target price to US\$20.10 from US\$20.70. Our new target price is based on an unchanged 2020E P/E multiple of 12x and revised non-GAAP diluted EPADS of US\$1.67 (down from US\$1.73), and is down 3% from our previous target price of US\$20.70, indicating 43% upside potential from the March 13 closing price of US\$14.00.

Exhibit 3 - Peer comparison table

Company name	Ticker	Rating	Price 3/13/2020	Mkt Cap (US\$ mn)	P/E Multiples			PEG		Rev Growth			EPS Growth		
					2019E	2020E	2021E	2019E	2020E	2019E	2020E	2021E	2019E	2020E	2021E
Huami Corp*	HMI US	BUY	USD 14.00	\$858	9.9x	8.3x	7.1x	0.5x	0.5x	59%	34%	11%	29%	19%	16%
Consumer electronic															
Garmin Ltd	GRMN US	NC	USD 77.34	\$14,748	15.4x	16.6x	16.2x	NM	5.9x	12%	6%	5%	36%	(7%)	3%
Logitech International SA	LOGI US	NC	USD 36.85	\$6,379	23.6x	17.5x	17.0x	0.7x	5.6x	9%	5%	6%	23%	35%	3%
iRobot Corp	IRBT US	NC	USD 40.98	\$1,162	13.5x	21.0x	15.3x	NM	0.6x	11%	9%	9%	(4%)	NA	37%
Viomi Technology	VIOT US	NC	USD 5.20	\$362	7.6x	5.5x	4.6x	0.2x	0.3x	71%	42%	43%	126%	39%	18%
GoPro Inc	GPRO US	NC	USD 2.72	\$346	NM	6.6x	6.4x	NM	1.7x	4%	(2%)	(1%)	NM	NM	4%
Mean					15.0x	13.4x	11.9x	0.4x	2.8x	21%	12%	12%	45%	22%	13%
Median					14.5x	16.6x	15.3x	0.4x	1.7x	11%	6%	6%	29%	35%	4%

Source: Bloomberg, Company data, CRSHK estimates. *CRSHK estimates, Bloomberg consensus for NC companies

Risks

- **The COVID-19 outbreak may last longer than expected.** If the COVID-19 outbreak lasts longer than we expect, it may harm Huami's shipments of both Xiaomi wearable products and self-branded products, dragging down the revenue generation capability of the company and impacting our target price.
- **Potential changes to Xiaomi agreement.** Xiaomi is Huami's most important customer and distribution channel. Any deterioration in the relationship between the two parties, or a decline in sales of Xiaomi Wearable Products could have a materially adverse effect on Huami's operating results. Although the cooperation agreement will be renewed after 2020 and termination is unlikely to happen after 2-3 years due to limited period of validity, in our view, it is possible that specific terms of the agreement (such as profit allocation model) could be modified.
- **Potential competition from Xiaomi.** Xiaomi recently launched its own smart watch, and there may be further product launches in 2020. If Xiaomi continues to launch different types of smart watches in the future, we expect Xiaomi to be a key competitor for Amazfit, Huami's self-branded products, and thus may bring downward pressure on Huami's performance.
- **Slower-than-expected technological development in healthcare-level sensors.** The current bottleneck for the smart wearables industry—and thus Huami—is the lack of healthcare-level sensors. Technological breakthroughs in this field, however, necessarily rely on the work of upstream sensor suppliers, making any developments or progress in this area very difficult to predict. There are risks that the launch of healthcare-level sensors will come later than expected.
- **Intensifying competition in China from local companies.** Although we do not think Huami would face direct competition from international peers focused on high-end products due to different pricing strategies and product positions, we do see a risk of domestic competitors such as Huawei (private), which possesses similar domestic supply chain advantages, threatening Huami's leading position in shipments.
- **Slower-than-expected overseas expansion.** Huami's overseas approach will be largely determined by the speed of Xiaomi's overseas expansion, especially in offline channels. Risks such as foreign regulation and local competition could constrain Xiaomi's pace to some extent.

Exhibit 4 - Quarterly income forecasts

Quarterly income forecast (RMBmn)	1Q19	2Q19	3Q19	4Q19E	1Q20E	2Q20E	3Q20E	4Q20E	1Q21E	2Q21E	3Q21E	4Q21E
Net revenue	800	1,039	1,863	2,111	1,137	1,436	2,441	2,773	1,302	1,637	2,694	3,046
COGS	582	761	1,393	1,608	831	1,044	1,804	2,071	940	1,190	1,996	2,245
Gross Profit	217	277	470	503	307	393	637	702	362	446	698	801
Gross margin	27.2%	26.7%	25.2%	23.8%	27.0%	27.3%	26.1%	25.3%	27.8%	27.3%	25.9%	26.3%
R&D Expense	72	94	125	140	85	108	183	208	98	123	202	228
General and Administrative Expenses	45	51	70	83	57	72	122	139	65	82	135	152
Sales/Marketing/Advertising Expenses	22	40	57	63	45	57	98	111	52	65	108	122
Operating Expense	140	185	251	285	188	237	403	457	215	270	445	503
Operating Income	78	92	219	218	119	156	234	244	147	176	254	298
Operating margin	9.7%	8.9%	11.8%	10.3%	10.5%	10.8%	9.6%	8.8%	11.3%	10.8%	9.4%	9.8%
Finance income (costs)	7.5	4.8	10.9	10.3	5.9	5.9	5.9	5.9	7.9	7.9	7.9	7.9
Other income (cost)	0.5	4.4	(2.0)	9.6	9.6	9.6	9.6	9.6	9.6	9.6	9.6	9.6
Pre-Tax income	86	101	228	237	135	171	250	260	165	194	271	316
Income tax benefit (expense)	10.7	12.4	27.5	27.3	15.5	19.7	28.7	29.9	18.9	22.3	31.2	36.3
Loss from equity method investments	0.0	(0.3)	2.9	(3.8)	-	-	-	-	-	-	-	-
Net income	75	89	203	206	119	161	221	230	146	171	240	279
Net margin	9.4%	8.5%	10.9%	9.8%	10.5%	10.5%	9.1%	8.3%	11.2%	10.5%	8.9%	9.2%
Non-GAAP net income	95	112	210	214	125	159	228	238	152	180	248	289
Non-GAAP net margin	11.9%	10.8%	11.3%	10.1%	11.0%	11.0%	9.4%	8.6%	11.7%	11.0%	9.2%	9.5%

Source: Company data, CRSHK estimates. Note: USD/RMB=7.0

Exhibit 5 - Annual income forecasts

Annual income forecast (RMBmn)	2017	2018	2019E	2020E	2021E	2022E
Net revenue	2,049	3,645	5,812	7,787	8,679	10,051
COGS	1,554	2,706	4,345	5,749	6,372	7,371
Gross Profit	495	939	1,468	2,038	2,307	2,680
Gross margin	24.1%	25.8%	25.3%	26.2%	26.6%	26.7%
R&D Expense	154	263	431	584	651	754
General and Administrative Expenses	115	214	248	389	434	503
Sales/Marketing/Advertising Expenses	44	97	182	311	347	402
Operating Expense	313	574	861	1,285	1,432	1,658
Operating Income	182	366	606	753	875	1,022
Operating margin	8.9%	10.0%	10.4%	9.7%	10.1%	10.2%
Finance income (costs)	3.0	11.6	33.5	23.4	31.7	40.8
Other income (cost)	6.9	9.3	12.4	38.3	38.3	38.3
Pre-Tax income	192	387	652	815	945	1,101
Income tax benefit (expense)	27.6	52.0	77.9	93.8	108.8	126.7
Loss from equity method investments	(2.8)	(1.7)	(1.1)	-	-	-
Net income	167	336	573	721	836	974
Net margin	8.2%	9.2%	9.9%	9.3%	9.6%	9.7%
Non-GAAP net income	230	475	630	750	868	1,011
Non-GAAP net margin	11.2%	13.0%	10.8%	9.6%	10.0%	10.1%
Non-GAAP EPADS (RMB)	3.62	7.59	9.81	11.72	13.57	15.80
Non-GAAP EPADS (US\$)	0.54	1.12	1.40	1.67	1.94	2.26

Source: Company data, CRSHK estimates. Note: USD/RMB=7.0

Appendix A

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Hold – The stock price of the subject company is not expected to either appreciate or depreciate meaningfully from the typical benchmark market index for the subject company's primary listing exchange (e.g. the S&P 500 for US-listed stocks) during the above-stated time horizon.

Sell – The expected return on the subject company's stock price should underperform the typical benchmark market index for the subject company's primary listing exchange (e.g. the S&P 500 for US-listed stocks) over the above-defined time horizon from the publishing date of the initiation of coverage or subsequent report announcing a rating change.

Not Rated – China Renaissance has removed the rating and, if applicable, the price target, for the subject company's stock because of either a lack of a sufficient fundamental basis or for legal, regulatory or policy reasons. The previous rating and, if applicable, the price target, should no longer be relied upon. An NR designation is not a recommendation or a rating.

Not Covered – a company for which China Renaissance research has not been published.

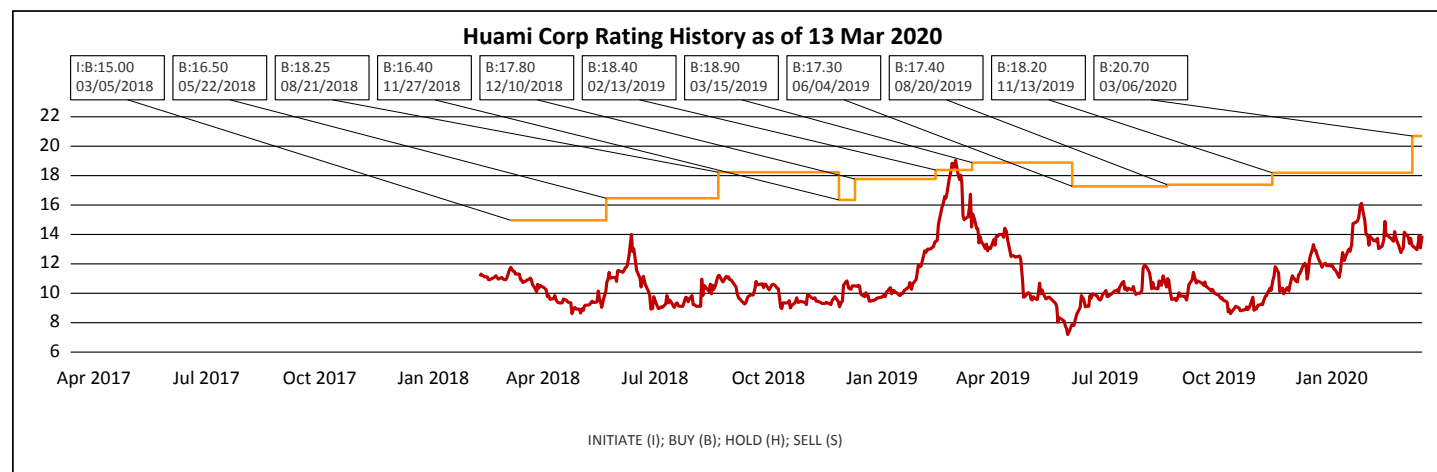
China Renaissance Ratings as of January 19, 2019:

Sector Ratings: Ratings of Overweight, Neutral and Underweight are applied to the designated sector coverage group with a time horizon of twelve to eighteen months from the date of report publication. The ratings are as follows:

Overweight – Expect sector to outperform the relevant market.

Neutral – Expect sector to perform in line with the relevant market.

Underweight – Expect sector to underperform the relevant market.



Valuation Methodology

HMI:

Based on a target 2020E PE of 12.0x and 2020E EPADS US\$1.67, our target price is US\$20.10.

Risks: 1) The COVID-19 outbreak may last longer than expected. 2) Potential changes to Xiaomi agreement. 3) Potential competition from Xiaomi. 4) Slower-than-expected technology development in healthcare-level sensors. 5) Intensifying competition in China from local companies. 6) Slower-than-expected overseas expansion.

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