

# Jiangsu Hengli Hydraulic (601100 CH)

## Short-term impact of power outage; Wait for more positive signals

We expect Hengli's production plan in Oct will be affected by the current power shortage, resulting in a slower-than-expected sales recovery in 4Q21E. We trim our earnings forecast in 2021E by 8%, to reflect lower volume and margin assumptions. We also revise down our earnings forecast by 4% each year in 2022E/23E to reflect our more conservative margin assumptions. Our TP is revised down from RMB103 to RMB86, based on 42x 2021E P/E which is equivalent to the historical average (previous target P/E: 46x). Maintain **HOLD**.

- **Scheduled production in Oct is affected by power shortage.** Hengli has scheduled production volume of 66k units of excavator hydraulic cylinder in Oct (up only 5% YoY but down 6% MoM), which is below our expectation. Scheduled production volume of large & medium size pump/valves also slowed to 8%/19% growth (YoY) in Oct. The conservative production plan is due to the uncertainties arising from power suspension.
- **3Q21E earnings preview.** Hengli will report the 3Q21E results on 25 Oct. We forecast net profit to slightly drop 3% YoY to RMB471mn, due to margin contraction that offset the revenue growth of 13%.
- **New business initiatives to drive diversification in terms of product offerings and international expansion.** Hengli is planning for a placement with a fund-raising size of RMB5bn (max). The proceeds will be mainly spent on the capacity expansion in Mexico (to support the global leading excavator manufacturer), as well as the new capacity of linear actuator for electric cylinder (a new area for potential import substitution). We are positive to Hengli's new business initiatives, given the excellent track record of achieving import substitution in the hydraulic cylinder, pump and valve.
- **Upside risks:** (1) Fast recovery of power supply; (2) better-than-expected excavator demand. **Downside risks:** (1) Continuous slowdown of construction activities; (2) longer-than-expected power suspension (3) risk of overseas expansion.

### Earnings Summary

(YE 31 Dec)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue (RMB mn)	5,414	7,855	9,854	10,883	11,601
YoY growth (%)	28.6	45.1	25.5	10.4	6.6
Net income (RMB mn)	1,296	2,254	2,686	3,173	3,563
EPS (RMB)	0.99	1.73	2.06	2.43	2.73
YoY growth (%)	54.9	73.9	19.2	18.1	12.3
Consensus EPS (RMB)	NA	NA	2.20	2.61	3.06
EV/EBITDA (x)	64.7	35.8	32.5	28.8	26.4
P/E (x)	84.2	48.4	40.6	34.4	30.6
P/B (x)	19.5	14.9	11.8	9.5	7.8
Yield (%)	0.5	0.7	0.9	1.0	1.1
ROE (%)	25.6	35.0	32.5	30.7	28.1
Net debt / equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIS estimates

**HOLD (Maintain)**

Target Price: **RMB86.00**  
 (Previous TP **RMB103.00**)  
 Up/Downside: **+3%**  
 Current Price: **RMB83.57**

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### Stock Data

Mkt Cap (RMB mn)	109,089
Avg 3 mths t/o (RMB mn)	937
52w High/Low (RMB)	137.66/67.50
Total Issued Shares (mn)	1,305

Source: Bloomberg

### Shareholding Structure

WANG's family	71.0%
CCASS (Hong Kong)	10.0%
Others	19.0%

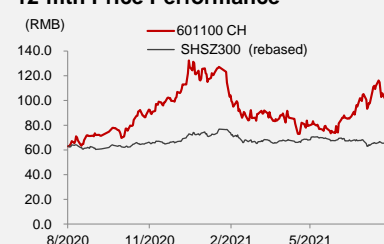
Source: Company data

### Share Performance

	Absolute	Relative
1-mth	-10.4%	-3.2%
3-mth	18.0%	27.0%
6-mth	-9.2%	6.6%

Source: Bloomberg

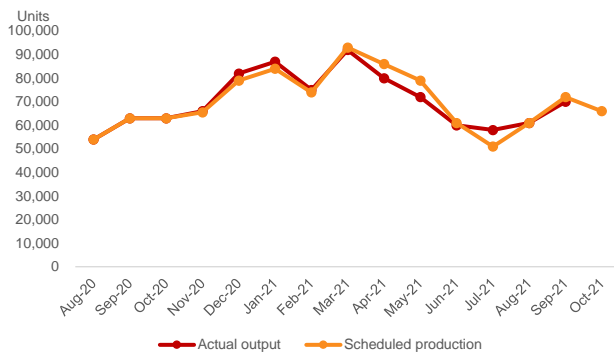
### 12-mth Price Performance



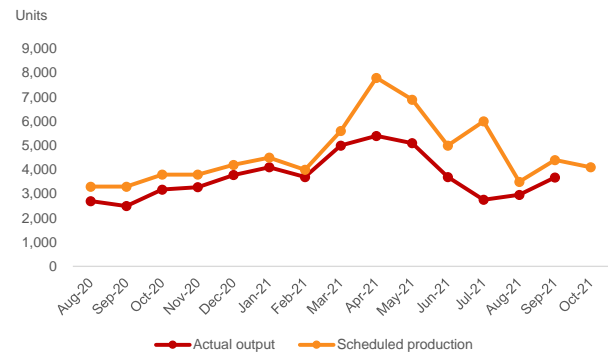
Source: Bloomberg

### Auditor: RSM

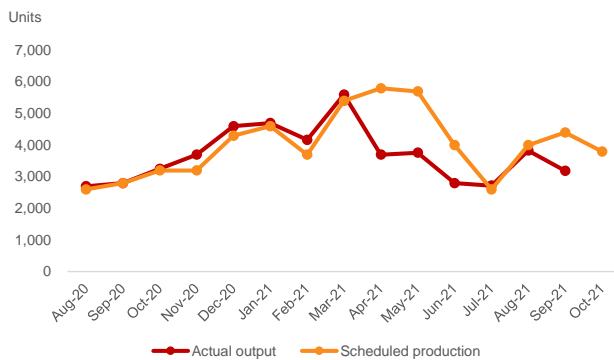
1. Jiangsu Hengli Hydraulic – Net profit in 2Q21 down only 2% YoY; better than expectations – 24 Aug 2021
2. Construction Machinery / HDT (Outperform) – Favourable policy shift; Defensive growth amid volatile market; Upgrade SANY Heavy & Sinotruk – 9 Aug 2021

**Figure 1: Hengli's hydraulic cylinders monthly production**

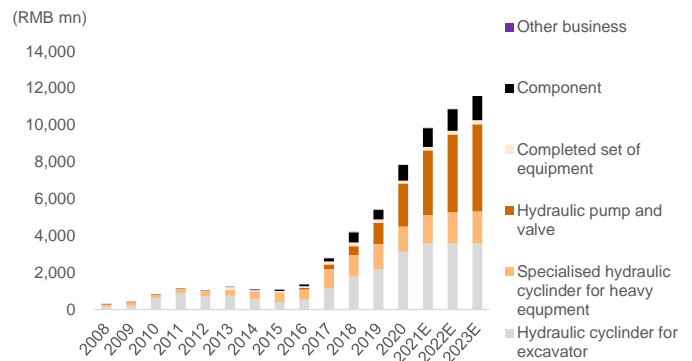
Source: Company data, CMBIS estimates

**Figure 2: Hengli's large & medium size pump monthly production**

Source: Company data, CMBIS estimates

**Figure 3: Hengli's hydraulic cylinders monthly production**

Source: Company data, CMBIS estimates

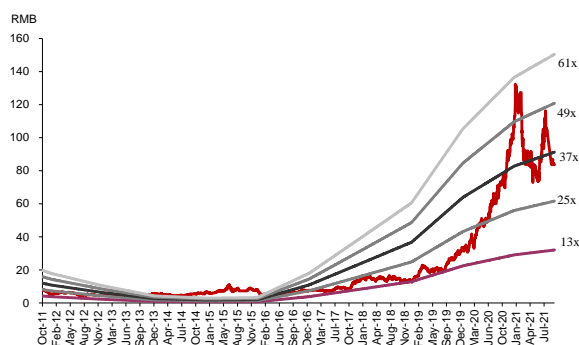
**Figure 4: Hengli's revenue breakdown**

Source: Company data, CMBIS estimates

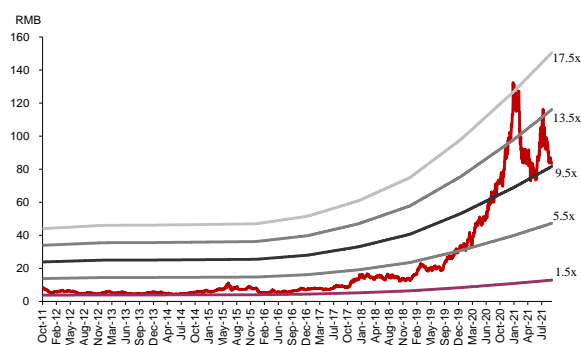
**Figure 5: Change in key assumptions**

(RMB mn)	Old			New			Change		
	2021E	2022E	2023E	2021E	2022E	2023E	2021E	2022E	2023E
<b>Revenue</b>									
Hydraulic cylinder for excavator	3,645	3,645	3,645	3,582	3,582	3,582	-1.7%	-1.7%	-1.7%
Specialised hydraulic cylinder for heavy equipment	1,563	1,720	1,771	1,539	1,693	1,744	-1.5%	-1.5%	-1.5%
Hydraulic pump and valve	3,624	4,168	4,585	3,508	4,209	4,714	-3.2%	1.0%	2.8%
Hydraulic system	196	216	237	191	211	232	-2.4%	-2.4%	-2.4%
Component	1,015	1,167	1,307	1,015	1,167	1,307	0.0%	0.0%	0.0%
<b>Revenue (hydraulic business)</b>	<b>10,044</b>	<b>10,916</b>	<b>11,546</b>	<b>9,835</b>	<b>10,862</b>	<b>11,579</b>	<b>-2.1%</b>	<b>-0.5%</b>	<b>0.3%</b>
Other business	19	21	22	19	21	22	0.0%	0.0%	0.0%
<b>Total revenue</b>	<b>10,063</b>	<b>10,936</b>	<b>11,567</b>	<b>9,854</b>	<b>10,883</b>	<b>11,601</b>	<b>-2.1%</b>	<b>-0.5%</b>	<b>0.3%</b>
<b>Gross margin</b>									
Hydraulic cylinder for excavator	41.0%	41.0%	41.0%	40.5%	40.5%	40.5%	-0.5	-0.5	-0.5
Specialised hydraulic cylinder for heavy equipment	39.0%	39.0%	39.0%	39.0%	39.0%	39.0%	0.0	0.0	0.0
Hydraulic pump and valve	44.0%	43.0%	43.0%	43.0%	43.0%	43.0%	-1.0	0.0	0.0
Hydraulic system	35.0%	35.0%	34.0%	35.0%	35.0%	34.0%	0.0	0.0	0.0
Component	20.0%	25.0%	33.0%	20.0%	25.0%	33.0%	0.0	0.0	0.0
<b>Gross margin (hydraulic business)</b>	<b>39.5%</b>	<b>39.6%</b>	<b>40.4%</b>	<b>38.9%</b>	<b>39.5%</b>	<b>40.3%</b>	<b>-0.6</b>	<b>-0.2</b>	<b>-0.1</b>
Other business	66.0%	66.0%	66.0%	66.0%	66.0%	66.0%	0.0	0.0	0.0
<b>Average gross margin</b>	<b>39.6%</b>	<b>39.7%</b>	<b>40.5%</b>	<b>39.0%</b>	<b>39.5%</b>	<b>40.4%</b>	<b>-0.6</b>	<b>-0.2</b>	<b>-0.1</b>
<b>Change (ppt)</b>									
S&D expense ratio	-1.2%	-1.2%	-1.2%	-1.1%	-1.1%	-1.1%	0.1	0.1	0.1
Admin expense and R&D ratio	-6.2%	-6.1%	-6.0%	-6.9%	-6.7%	-6.7%	-0.7	-0.6	-0.7
<b>Net profit</b>	<b>2,932</b>	<b>3,307</b>	<b>3,713</b>	<b>2,716</b>	<b>3,237</b>	<b>3,652</b>	<b>-7.4%</b>	<b>-2.1%</b>	<b>-1.7%</b>

Source: Company data, CMBIS estimates

**Figure 6: Hengli's P/E band**

Source: Bloomberg, Company data, CMBIS estimates

**Figure 7: Hengli's P/B band**

Source: Bloomberg, Company data, CMBIS estimates

## Financial Summary

### Income statement

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Total revenue</b>	<b>5,414</b>	<b>7,855</b>	<b>9,854</b>	<b>10,883</b>	<b>11,601</b>
Cost of sales	(3,369)	(4,391)	(6,012)	(6,583)	(6,918)
<b>Gross profit</b>	<b>2,045</b>	<b>3,464</b>	<b>3,842</b>	<b>4,300</b>	<b>4,683</b>
Surcharge	(52)	(72)	(89)	(98)	(104)
S&D expenses	(111)	(107)	(108)	(120)	(128)
Administrative expenses	(435)	(509)	(680)	(729)	(777)
Asset impairment	(52)	(90)	0	0	0
<b>EBIT</b>	<b>1,395</b>	<b>2,687</b>	<b>2,965</b>	<b>3,353</b>	<b>3,673</b>
Net finance income/(cost)	31	(151)	131	309	465
Finance income	187	223	239	357	511
Finance expenses	(156)	(375)	(109)	(48)	(46)
Other gains/(losses)	67	74	69	109	116
Profit of JV and associates	0	0	0	0	0
<b>Pretax profit</b>	<b>1,493</b>	<b>2,609</b>	<b>3,164</b>	<b>3,771</b>	<b>4,255</b>
Income tax	(195)	(348)	(443)	(528)	(596)
<b>After tax profit</b>	<b>1,298</b>	<b>2,261</b>	<b>2,721</b>	<b>3,243</b>	<b>3,659</b>
MI	(2)	(7)	(5)	(6)	(7)
<b>Net profit</b>	<b>1,296</b>	<b>2,254</b>	<b>2,716</b>	<b>3,237</b>	<b>3,652</b>
D&A	264	311	338	369	394
<b>EBITDA</b>	<b>1,659</b>	<b>2,997</b>	<b>3,303</b>	<b>3,722</b>	<b>4,067</b>

### Cash flow summary

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Pretax profit	1,493	2,609	3,129	3,697	4,152
Finance cost	-33	146	109	68	68
Profit or loss of associates	0	0	0	0	0
Loss/(gain) on disposal	1	1	0	0	0
Depreciation & amortization	264	311	338	369	394
Income tax paid	-375	-714	-438	-518	-581
Change in working capital	66	-849	-321	-64	-181
Others	253	488	0	0	0
<b>Cash flow from operation</b>	<b>1,660</b>	<b>1,981</b>	<b>2,818</b>	<b>3,552</b>	<b>3,852</b>
Net capex on PP&E	-434	-380	-500	-500	-400
Investment in JV/associates	0	0	0	0	0
Investment in subsidiaries	0	0	0	0	0
Investment in intangibles	-4	-19	-20	-20	-20
Dividend received	0	0	0	0	0
Others	-14	-264	0	0	0
<b>Cash flow from investing</b>	<b>-452</b>	<b>-663</b>	<b>-520</b>	<b>-520</b>	<b>-420</b>
Equity financing/(repurchase)	0	0	0	0	0
Net bank borrowings	-100	-361	-150	0	0
Dividend paid	-265	-529	-783	-940	-1,110
Interest paid	-107	-40	-109	-68	-68
Others	18	112	0	0	0
<b>Cash flow from financing</b>	<b>-454</b>	<b>-818</b>	<b>-1,042</b>	<b>-1,008</b>	<b>-1,179</b>
Change in cash	754	499	1,255	2,024	2,253
Cash at beginning of the year	1,571	2,343	2,777	4,033	6,056
Exchange and others	18	-66	0	0	0
Cash at the end of the year	2,343	2,777	4,033	6,056	8,310

### Balance sheet

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Non-current assets</b>	<b>2,935</b>	<b>3,025</b>	<b>3,207</b>	<b>3,358</b>	<b>3,384</b>
PP&E	2,364	2,432	2,608	2,753	2,774
JV/associates	0	0	0	0	0
Goodwill	0	0	0	0	0
Intangible assets	273	280	286	292	297
AFS investments	0	0	0	0	0
Others	257	261	261	261	261
Deferred tax assets	41	52	52	52	52
<b>Current assets</b>	<b>5,492</b>	<b>7,595</b>	<b>9,545</b>	<b>11,581</b>	<b>14,218</b>
Inventories	997	1,217	1,814	1,468	1,943
Trade and bill receivables	1,639	2,705	2,803	3,160	3,069
Prepayment	98	164	164	164	164
Others	414	733	733	733	733
Pledged deposits	0	0	0	0	0
Cash	2,343	2,777	4,033	6,056	8,310
<b>Current liabilities</b>	<b>2,170</b>	<b>2,590</b>	<b>2,864</b>	<b>2,812</b>	<b>3,015</b>
Trade and bill payables	791	1,131	1,505	1,453	1,656
Bank borrowings	937	554	454	454	454
Tax payable	62	119	119	119	119
Advance from customers	192	108	108	108	108
Others	188	677	677	677	677
<b>Non-current liabilities</b>	<b>643</b>	<b>679</b>	<b>629</b>	<b>629</b>	<b>629</b>
Bank borrowings	200	370	320	320	320
Deferred tax liabilities	70	108	108	108	108
Deferred income	223	200	200	200	200
Others	150	0	0	0	0
<b>Equity</b>	<b>5,614</b>	<b>7,352</b>	<b>9,260</b>	<b>11,499</b>	<b>13,959</b>
Shareholders' equity	5,584	7,314	9,216	11,449	13,902
MI	30	38	43	50	57

### Key ratios

YE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Sales mix (%)</b>					
Cylinder for excavator	40%	40%	36%	33%	31%
Cylinder for heavy equipment	25%	17%	16%	16%	15%
Hydraulic pump and valve	21%	30%	36%	39%	41%
Hydraulic system	3%	2%	2%	2%	2%
Component	9%	11%	10%	11%	11%
Other business	0%	0%	0%	0%	0%
Total revenue	100%	100%	100%	100%	100%
<b>Profit &amp; loss ratio (%)</b>					
Gross margin	37.8	44.1	39.0	39.5	40.4
EBIT margin	25.8	34.2	30.1	30.8	31.7
Net profit margin	24.0	28.8	27.3	29.2	30.8
<b>Growth (%)</b>					
Revenue	28.6	45.1	25.5	10.4	6.6
Gross profit	32.7	69.4	10.9	11.9	8.9
EBIT	58.7	92.7	10.3	13.1	9.5
Net profit	54.9	73.9	19.2	18.1	12.3
<b>Balance sheet ratio</b>					
Current ratio (x)	2.5	2.9	3.3	4.1	4.7
Receivable turnover days	100	101	102	100	98
Inventory turnover days	111	92	92	91	90
Payable turnover days	80	80	80	82	82
Net debt / total equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash
<b>Profitability (%)</b>					
ROA	16.5	23.7	23.0	22.9	21.9
ROE	25.6	35.0	32.5	30.7	28.1
<b>Per share data</b>					
EPS (RMB)	0.99	1.73	2.06	2.43	2.73
BVPS (RMB)	4.28	5.60	7.06	8.77	10.65
DPS (RMB)	0.41	0.60	0.72	0.85	0.96

Source: Company data, CMBIS estimates

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