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Yonyou (600588 CH)

Takes time to build the cloud platform

Yonyou reported better than expected FY2Q22 with steady revenue growth of +15% YoY to RMB2.26bn. Cloud revenue grew +57% YoY to RMB1.55bn. However, we observed ARR/ contract liabilities growth have slowed to +2%/ +11% HoH. These may suggest a decline in renewal rate and add pressure to Yonyou's cloud subscription business. Meanwhile, Yonyou increased R&D in cloud platform YonBIP targeting large-sized enterprises. R&D was up +38% YoY, as well as R&D capitalization rate. We think earnings quality will be distorted during the YonBIP ramp up phase. Maintain HOLD.

- **FY2Q22 beat on lower opex ratio.** Yonyou delivered steady top-line growth at +15% YoY to RMB2,258mn, beating our/ consensus estimates by 9%/2%. Cloud revenue was RMB1,551mn (+57% YoY, +107% QoQ), accounting for 69% of total. Operating profit was RMB89mn (+34% YoY), lower opex ratio at 57.3% (-2.7 pcts) has offset decline in GPM (-2.1 pcts YoY to 61.2%). Net profit was RMB137mn (-40% YoY).
- **ARR/ contract liabilities HoH growth slowdown adds uncertainty to cloud outlook.** In FY1H22, Yonyou cloud revenue grew +53% YoY to RMB2,299mn. In terms of customer mix, 67/ 18% of cloud revenue came from large-sized/ SME enterprises. ARR was RMB1,680mn (+102% YoY, +2% HoH). Cloud contract liabilities was RMB1,760mn (+42% YoY, +11% HoH). These cloud metrics look good on a YoY basis but HoH growth rates slowed. These may suggest a decline in renewal rate and we are concerned that Yonyou's subscription revenue (mostly derived from SME) growth may slow down.
- **Increasing R&D (and capitalization rate) related to YonBIP platform for large-size enterprises.** In FY1H22, Yonyou increased R&D expenditure by 38% YoY to RMB1.32bn as the Company continues to develop cloud-native YonBIP platform for large-sized enterprises. R&D capitalization rate also rose to 26.4% (vs. 21.9% in FY1H21). We think earnings quality will be distorted in the short term during YonBIP ramp-up stage.
- **Maintain HOLD.** We raised FY22-24E net profit by 1-5% to reflect better than expected opex control. Maintain HOLD with new target price of RMB19.81 (prior RMB19.58), based on unchanged 5.0x FY23E EV/sales.

Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (RMB mn)	8,525	8,932	10,382	12,709	15,031
YoY growth (%)	0%	5%	16%	22%	18%
Net profit (RMB mn)	989	708	686	959	1,275
EPS (RMB)	0.30	0.22	0.20	0.28	0.37
YoY growth (%)	-17%	-28%	-8%	40%	33%
Consensus EPS (RMB)	0.30	0.22	0.21	0.31	0.45
EV/sales (x)	8.0	7.8	6.5	5.2	4.2
P/E (x)	67.5	94.2	102.0	73.0	54.9
Dividend Yiled (%)	0.01	0.01	0.00	0.00	0.00
ROE (%)	12%	9%	7%	7%	9%
Net debt to equity	net cash	net cash	net cash	net cash	net cash

Source: Company data, Bloomberg, CMBIGM estimates

Hold (Maintain)

Target Price	RMB19.81
(Previous TP	RMB19.58)
Up/Downside	-2.9%
Current Price	RMB20.39

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Stock Data

Mkt Cap (RMB mn)	70,017
Avg 3 mths t/o (RMB mn)	630.18
52w High/Low (RMB)	40.33/ 16.53
Total Issued Shares (mn)	3,434

Source: Bloomberg

Shareholding Structure

Mr. Wang- Chairman	41.2%
HKSCC	7.3%
Mr. Guo - Vice Chairman	3.7%

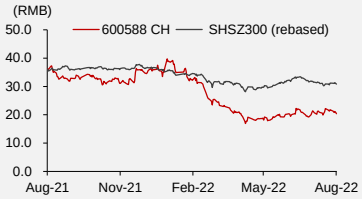
Source: Company data

Share Performance

	Absolute	Relative
1-mth	4.3%	7.1%
3-mth	10.8%	5.8%
6-mth	-35.1%	-27.8%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

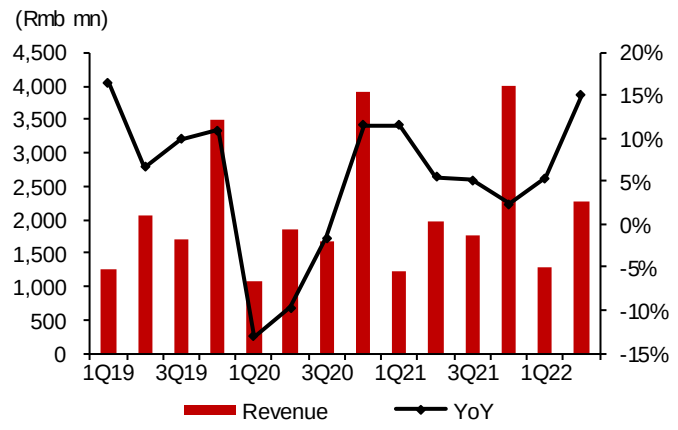
Auditor: Deloitte

Related Reports

1. China Software & IT Services "A mixed outlook for China Cloud amid rising US-China tension" – 4 Aug 2022 (link)
2. China Software & IT Services "Higher visibility in SaaS along China cloud value chain" – 28 Jun 2022 (link)
3. China Software & IT Services "Software localization to benefit China ERP" – 27 May 2022 (link)

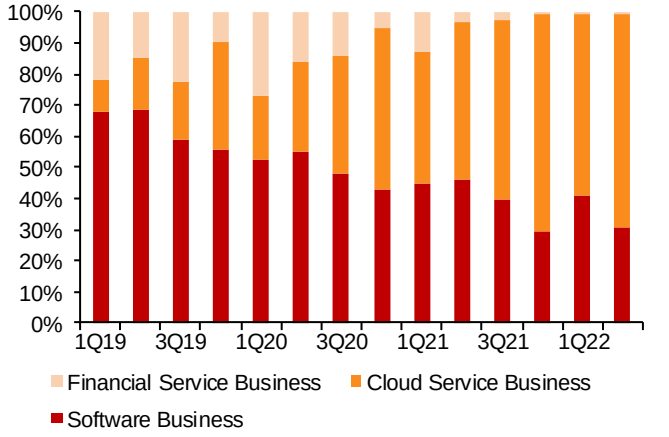
Focus Charts

Figure 1: Revenue and growth (Quarterly)



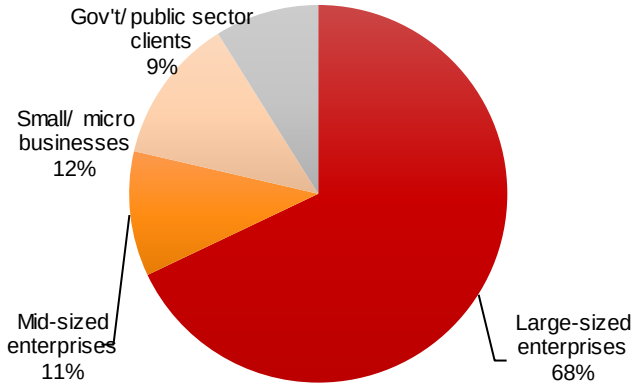
Source: Company data, CMBIGM estimates

Figure 2: Revenue mix (Quarterly)



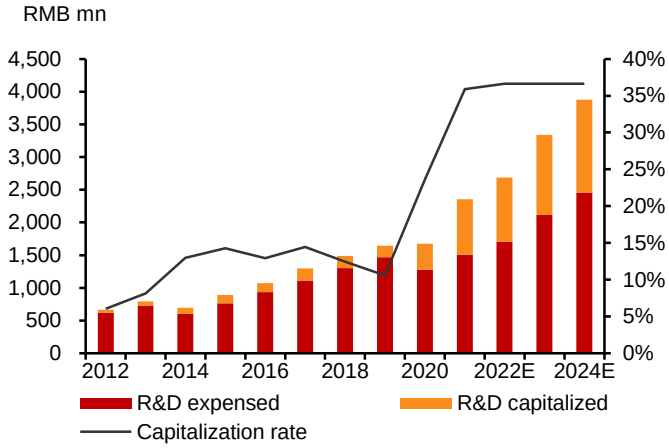
Source: Company data, CMBIGM estimates

Figure 3: Cloud service revenue mix (1H22)



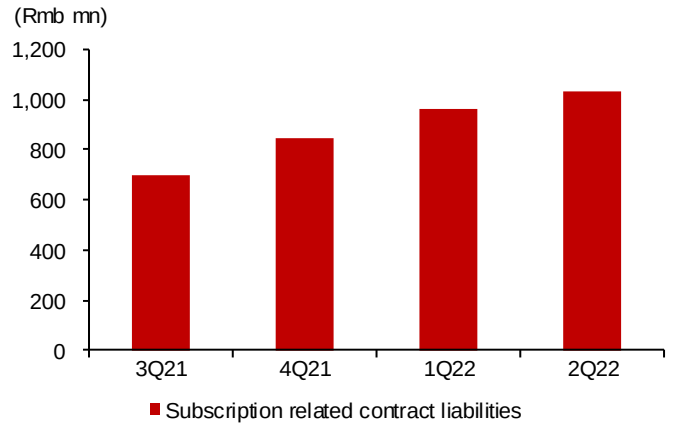
Source: Company data, CMBIGM estimates

Figure 4: R&D capitalization rate (Yearly)



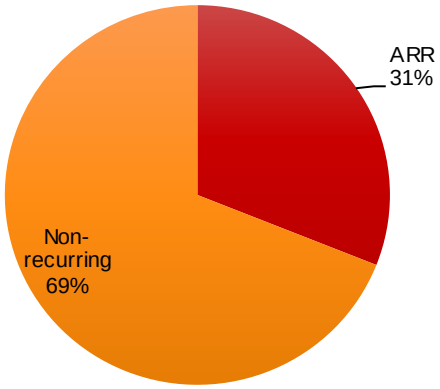
Source: Company data, CMBIGM estimates

Figure 5: Cloud contract liabilities (Quarterly)



Source: Company data

Figure 6: ARR as % of cloud service revenue



Source: Company data

FY2Q22 results review

- **Revenue** was RMB2,258mn (+15% YoY, +76% QoQ), beating our estimate by 9% and consensus by 2%. *(pre-announced revenue: RMB2,229-2,288mn)*
  - **Cloud** revenue was RMB1,551mn (+57% YoY, +107% QoQ), accounting for 69% of revenue.
  - **Software** revenue was RMB690mn (-24% YoY, +32% QoQ).
- **Gross profit** was RMB1,383 (+11%YoY, +120% QoQ), beating our estimate by 12% and consensus by 4%.
- **Gross margin** was 61.2%, (-2.1 pct pts YoY, +12.1 pct pts QoQ), beating our estimate by 1.8 pct pts and consensus by 1 pct pts.
- **Operating profit** was RMB89mn (+34% YoY, +119% QoQ), beating our estimate
- **Operating margin** was 4.0% (+0.6 pct pts YoY, +40.3 pct pts QoQ), beating our estimate by 7.1 pct pts.
- **Net profit** was RMB137mn (-40% YoY, +135% QoQ), beating our estimate/ consensus estimates *(pre-announced net profit: RMB120-150mn)*
- **EPS** was RMB0.04 (-43% YoY, +134% QoQ).

Figure 7: FY2Q22 results review

	Jun-21 2Q21	Mar-22 1Q22	Jun-22 2Q22			Jun-22 2Q22		Jun-22 2Q22	
RMB mn	**actual**	**actual**	**actual**	**YoY**	**QoQ**	**CMBI**	**versus CMBI**	**consensus**	**versus consensus**
Revenue	1,963	1,279	2,258	15%	76%	2,078	9%	2,210	2%
Gross profit	1,244	628	1,383	11%	120%	1,236	12%	1,332	4%
Gross margin	63.4%	49.1%	61.2%	-2.1 pct pts	12.1 pct pts	59.5%	1.8 pct pts	60.3%	1 pct pts
Operating profit (adjusted)	67	-465	89	34%	119%	-64	n.a.	n.a.	0%
Operating margin (adjusted)	3.4%	-36.4%	4.0%	0.6 pct pts	40.3 pct pts	-3.1%	7.1 pct pts	n.a.	0.0%
Net non-op	126	41	20			59		n.a.	
PBT	192	-424	110	-43%	126%	-5	n.a.	131	-16%
Tax	-2	-1	-2			0		-7	
Minorities	37	32	30			0			
Net income	228	-393	137	-40%	135%	-4	n.a.	124	11%
EPS (RMB)	0.07	-0.12	0.04	-43%	134%	0.00	n.a.	0.02	82%

Source: Company data, CMBIGM

Figure 8: Revenue breakdown

RMB mn	1Q20	2Q20	3Q20	4Q20	1Q21	2Q21	3Q21	4Q21	1Q22	2Q22
Software	564	1,023	797	1,660	542	903	692	1,183	522	690
Cloud Service	219	532	630	2,042	516	990	1,020	2,794	748	1,551
Financial Service	293	294	229	189	156	70	44	22	9	17
Total	**1,089**	**1,862**	**1,669**	**3,905**	**1,214**	**1,963**	**1,756**	**3,999**	**1,279**	**2,258**
YoY %										
Software	-33%	-27%	-20%	-15%	-4%	-12%	-13%	-29%	-4%	-24%
Cloud Service	74%	54%	103%	72%	136%	86%	62%	37%	45%	57%
Financial Service	8%	-1%	-40%	-45%	-47%	-76%	-81%	-89%	-94%	-76%
Total	**-13%**	**-10%**	**-2%**	**12%**	**11%**	**5%**	**5%**	**2%**	**5%**	**15%**
Revenue mix										
Software	52%	55%	48%	42%	45%	46%	39%	30%	41%	31%
Cloud Service	20%	29%	38%	52%	42%	50%	58%	70%	58%	69%
Financial Service	27%	16%	14%	5%	13%	4%	2%	1%	1%	1%
Cloud service metrics										
Cloud Service contract liab.				1,091	1,229	1,243	1,304	1,580	1,715	1,760
- Subscription contract liab.				473	492	n.a.	702	847	961	1,030
YoY								79%	96%	n.a.

Source: Company data

Earnings revision

Figure 9: Yonyou earnings revision

RMB mn	2022E New	2022E Old	2022E %Diff	2023E New	2023E Old	2023E %Diff	2024E New	2024E Old	2024E %Diff
Sales	10,382	10,202	2%	12,709	12,478	2%	15,031	14,738	2%
Gross profit	6,318	6,172	2%	7,785	7,619	2%	9,287	9,066	2%
OP Profit	636	590	8%	959	913	5%	1,331	1,266	5%
PBT	788	799	-1%	1,128	1,122	1%	1,500	1,486	1%
Net profit	686	652	5%	959	954	1%	1,275	1,263	1%
EPS	0.20	0.19	5%	0.28	0.28	1%	0.37	0.37	1%
Margins									
GM	60.9%	60.5%	37 bps	61.3%	61.1%	19 bps	61.8%	61.5%	27 bps
OPM	6.1%	5.8%	33 bps	7.5%	7.3%	23 bps	8.9%	8.6%	26 bps
PBT margin	7.6%	7.8%	-24 bps	8.9%	9.0%	-11 bps	10.0%	10.1%	-10 bps
Net margin	6.6%	6.4%	22 bps	7.5%	7.6%	-10 bps	8.5%	8.6%	-9 bps

Source: Company data, CMBIGM

Figure 10: Yonyou CMBI estimates vs. consensus

RMB mn	2022E CMBI	2022E Street	2022E Diff	2023E CMBI	2023E Street	2023E Diff	2024E CMBI	2024E Street	2024E Diff
Sales	10,382	10,627	-2%	12,709	13,097	-3%	15,031	16,203	-7%
Gross profit	6,318	6,470	-2%	7,785	7,997	-3%	9,287	9,908	-6%
OP Profit	636	939	-32%	959	1,272	-25%	1,331	1,695	-21%
PBT	788	798	-1%	1,128	1,187	-5%	1,500	1,699	-12%
Net profit	686	720	-5%	959	1,046	-8%	1,275	1,483	-14%
EPS	0.20	0.21	-4%	0.28	0.31	-10%	0.37	0.44	-16%
Margins									
GM	60.9%	60.9%	-3 bps	61.3%	61.1%	19 bps	61.8%	61.1%	64 bps
OPM	6.1%	8.8%	-271 bps	7.5%	9.7%	-217 bps	8.9%	10.5%	-161 bps
PBT margin	7.6%	7.5%	8 bps	8.9%	9.1%	-19 bps	10.0%	10.5%	-50 bps
Net margin	6.6%	6.8%	-16 bps	7.5%	8.0%	-44 bps	8.5%	9.2%	-67 bps

Source: Company data, CMBIGM, Bloomberg

Operating model

Figure 11: Revenue breakdown

RMB mn	2019	2020	2021	2022E	2023E	2024E
Revenues	8,510	8,525	8,932	10,382	12,709	15,031
Cost of sales	(2,942)	(3,321)	(3,461)	(4,064)	(4,924)	(5,744)
Gross Profit	5,567	5,204	5,471	6,318	7,785	9,287
Gross margin	65.4%	61.0%	61.2%	60.9%	61.3%	61.8%
R&D	(1,630)	(1,459)	(1,704)	(2,023)	(2,500)	(2,967)
SG&A	(3,023)	(2,496)	(3,099)	(3,497)	(4,147)	(4,765)
Operating Income	802	1,093	555	636	959	1,331
Operating margin	*9.4%*	*12.8%*	*6.2%*	*6.1%*	*7.5%*	*8.9%*
Non-Operating Income	602	33	219	152	169	170
Profit Before Tax	1,404	1,126	774	788	1,128	1,500
Income tax (expense) gain	(83)	(75)	(92)	(107)	(113)	(150)
Minorities	(138)	(63)	25	6	(56)	(75)
Net Income to Shareholders	1,183	989	708	686	959	1,275
Net margin	13.9%	11.6%	7.9%	6.6%	7.5%	8.5%
EPS (RMB)	0.36	0.30	0.22	0.20	0.28	0.37
DPS (RMB)	0.15	0.20	0.20	0.00	0.00	0.00

Source: Company data, CMBIGM

Figure 12: Operating model

RMB mn	2019	2020	2021	2022E	2023E	2024E
Revenue breakdown						
Software Business	5,195	4,044	3,320	2,806	2,440	2,195
Cloud Service Business	1,970	3,422	5,321	7,551	10,269	12,836
Financial Service Business	1,293	1,005	276	26	-	-
Others	52	54	14	-	-	-
Total	8,510	8,525	8,932	10,382	12,709	15,031
Revenue YoY						
Software Business	-7%	-22%	-18%	-15%	-13%	-10%
Cloud Service Business	132%	74%	55%	42%	36%	25%
Financial Service Business	4%	-22%	-73%	-91%	-100%	0%
Blended	10%	0%	5%	16%	22%	18%
Revenue mix						
Software Business	61%	47%	37%	27%	19%	15%
Cloud Service Business	23%	40%	60%	73%	81%	85%
Financial Service Business	15%	12%	3%	0%	0%	0%

Source: Company data, CMBIGM

Figure 13: Quarterly operating model

RMB mn	1Q21	2Q21	3Q21	4Q21	1Q22	2Q22	3Q22E	4Q22E
Revenues	1,214	1,963	1,756	3,999	1,279	2,258	2,067	4,778
Gross Profit	572	1,244	1,020	2,634	628	1,383	1,155	3,153
Operating profit	-314	67	-124	926	-465	89	-179	1,191
Net profit (loss)	-13	228	-88	581	-393	137	-112	1,054
EPS (RMB)	-0.00	0.07	-0.03	0.18	-0.12	0.04	-0.03	0.31
Margins								
Gross margin	47%	63%	58%	66%	49%	61%	56%	66%
Operating margin	-26%	3%	-7%	23%	-36%	4%	-9%	25%
Net margin	-1%	12%	-5%	15%	-31%	6%	-5%	22%
Growth (QoQ)								
Revenues	-69%	62%	-11%	128%	-68%	76%	-8%	131%
Gross Profit	-79%	118%	-18%	158%	-76%	120%	-16%	173%
Operating profit	-127%	-121%	-287%	-846%	-150%	-119%	-301%	-764%
Net profit (loss)	-101%	-1858%	-139%	-759%	-168%	-135%	-181%	-1041%
Growth (YoY)								
Revenues	11%	5%	5%	2%	5%	15%	18%	19%
Gross Profit	13%	15%	9%	-2%	10%	11%	13%	20%
Operating profit	-9%	-72%	-214%	-22%	-48%	34%	-44%	29%
Net profit (loss)	95%	-14%	-113%	-42%	-2856%	-43%	-21%	73%

Source: Company data, CMBIGM

Valuation

Yonyou (600588 CH, HOLD, TP RMB19.81)

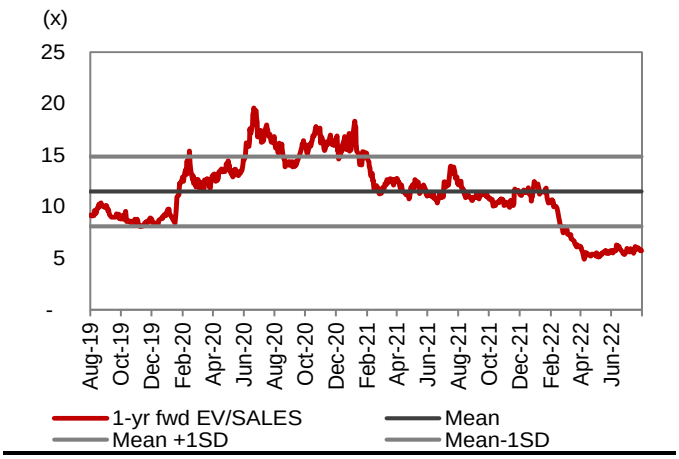
We maintain HOLD with new target price of RMB19.81 (prior RMB19.58), based on unchanged 5.0x FY23E EV/sales (40% discount to global enterprise SaaS person lower subscription revenue contribution). Yonyou is trading at three-year low but we believe re-rating would be difficult in the short term given that 80% of its cloud revenue is derived from large-enterprises who are less willing to accept subscription model and require higher customization work.

Figure 14: Yonyou peers valuation comparison

Company	Ticker	Rating	Market Cap (US$ mn)	Price (LC)	TP (LC)	EV/sales (x) FY22E	EV/sales (x) FY23E	FCF margin (%) FY22E	FCF margin (%) FY23E	Sales CAGR FY21-24E	EPS CAGR FY21-24E
Yonyou	600588 CH	HOLD	10,279	20.39	19.81	6.5	5.2	0%	7%	19%	20%
Kingdee	268 HK	BUY	7,095	16.02	23.83	9.1	7.5	-2%	1%	19%	n.a.
Kingsoft Office	688111 CH	NR	11,519	170.12	N/A	17.1	13.0	33%	38%	30%	31%
SAP	SAP US	NR	113,588	92.46	N/A	4.1	3.8	11%	15%	9%	n.a.
Intuit	INTU US	NR	134,764	477.76	N/A	10.9	9.5	29%	30%	20%	29%
Xero	XRO AU	NR	9,201	88.80	N/A	13.7	10.8	-7%	2%	25%	70%
Workday	WDAY US	NR	43,919	173.13	N/A	8.2	6.8	26%	18%	20%	n.a.
ServiceNow	NOW US	NR	98,899	489.60	N/A	13.3	10.7	30%	31%	24%	115%
Salesforce	CRM US	NR	186,990	187.93	N/A	7.1	5.9	19%	21%	20%	9%
					Mean	**10.0**	**8.1**	**15%**	**18%**	**21%**	**45%**
					Median	**9.1**	**7.5**	**19%**	**18%**	**20%**	**30%**

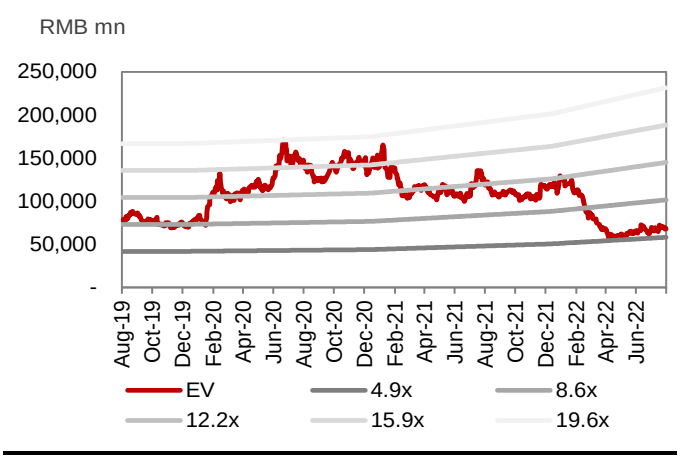
Source: Bloomberg, CMBIGM estimates

Figure 15: Yonyou 12M forward EV/sales chart



Source: Bloomberg, CMBIGM estimates

Figure 16: Yonyou 12M forward EV/sales band



Source: Bloomberg, CMBIGM estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	**8,525**	**8,932**	**10,382**	**12,709**	**15,031**
Cost of sales	(3,321)	(3,461)	(4,064)	(4,924)	(5,744)
Gross profit	**5,204**	**5,471**	**6,318**	**7,785**	**9,287**
Selling exp	(1,537)	(2,027)	(2,289)	(2,690)	(3,076)
Admin exp	(959)	(1,072)	(1,207)	(1,457)	(1,689)
R&D exp	(1,459)	(1,704)	(2,023)	(2,500)	(2,967)
Other operating exp.	(156)	(113)	(163)	(179)	(224)
Operating profit	**1,093**	**555**	**636**	**959**	**1,331**
Finance costs	(110)	(79)	(10)	-	-
Other non-oper exp.	143	298	161	169	170
Pre-tax profit	**1,126**	**774**	**788**	**1,128**	**1,500**
Income tax expense	(75)	(92)	(107)	(113)	(150)
Minority interests	(63)	25	6	(56)	(75)
Net profit to shareholders	**989**	**708**	**686**	**959**	**1,275**

Cash flow summary

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Net profit	**989**	**708**	**686**	**959**	**1,275**
Depreciation/amortization	357	473	526	671	852
Change in working capital	605	146	(155)	759	581
Others	(337)	(23)	158	56	75
Net cash from operating	**1,613**	**1,304**	**1,215**	**2,445**	**2,784**
Capex	(592)	(1,030)	(1,211)	(1,507)	(1,765)
Other	(183)	921	(3,087)	575	751
Net cash from investing	**(894)**	**(1,230)**	**(4,298)**	**(933)**	**(1,014)**
Net borrowings	(1,950)	702	1,017	153	(83)
Dividend paid	(651)	(654)	-	-	-
Other	346	(1,108)	6,287	(56)	(75)
Net cash from financing	**(2,256)**	**(1,060)**	**7,304**	**96**	**(158)**
Net change in cash	**(1,536)**	**(987)**	**4,221**	**1,608**	**1,612**
Cash at beginning of the year	7,147	5,605	4,616	8,261	9,869
Exchange difference	(6)	(2)	(4)	-	-
Cash at the end of the year	**5,605**	**4,616**	**8,833**	**9,869**	**11,481**

Balance sheet

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Current assets	**8,773**	**7,682**	**12,567**	**14,995**	**17,431**
Cash & equivalents	5,605	4,616	8,261	9,869	11,481
Account receivables	1,680	1,572	2,257	2,633	3,237
Inventory	423	407	409	667	728
Other current assets	1,065	1,088	1,640	1,826	1,986
Non-current assets	**8,177**	**9,647**	**11,312**	**11,574**	**11,735**
PPE	2,507	2,529	2,680	2,820	2,998
Intangible assets	785	1,862	2,447	3,144	3,879
Other non-current assets	4,885	5,256	6,184	5,610	4,859
Total assets	**16,950**	**17,329**	**23,878**	**26,569**	**29,167**
Current liabilities	**7,950**	**8,325**	**9,901**	**11,618**	**12,951**
ST borrowings	2,420	2,802	3,746	3,884	3,811
Account payables	549	654	760	905	1,068
Accrued expense	2,741	2,649	3,520	3,787	4,608
Other current liabilities	2,240	2,219	1,875	3,042	3,464
Non-current liabilities	**453**	**1,078**	**1,189**	**1,203**	**1,193**
LT borrowings	-	390	490	505	495
Other non-current liabilities	453	688	698	698	698
Total liabilities	**8,403**	**9,403**	**11,090**	**12,821**	**14,144**
Share capital	3,270	3,271	3,435	3,435	3,435
Capital surplus	1,096	892	6,065	6,065	6,065
Retained earnings	3,418	3,489	3,836	4,795	6,070
Other reserves	(242)	(664)	(1,398)	(1,398)	(1,398)
Minority interest	**1,004**	**939**	**961**	**961**	**961**
Total equity	**8,547**	**7,926**	**12,898**	**13,857**	**15,133**
Total liabilities and equity	**16,950**	**17,329**	**23,988**	**26,679**	**29,277**

Key ratios

YE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue mix					
Software Business	47%	37%	27%	19%	15%
Cloud Service Business	40%	60%	73%	81%	85%
Financial Service Business	12%	3%	0%	0%	0%
Growth (%)					
Revenue	0%	5%	16%	22%	18%
Operating profit	36%	-49%	15%	51%	39%
EPS	-17%	-28%	-8%	40%	33%
Profit & loss ratio (%)					
Gross margin	61.0%	61.2%	60.9%	61.3%	61.8%
Operating margin	12.8%	6.2%	6.1%	7.5%	8.9%
Net profit margin	11.6%	7.9%	6.6%	7.5%	8.5%
Balance sheet ratio					
Current ratio (x)	1.10	0.92	1.27	1.29	1.35
Receivable turnover days	77	66	67	70	71
Inventory turnover days	10	17	14	15	17
Payable turnover days	60	69	68	26	26
Net debt to equity	net cash	net cash	net cash	net cash	net cash
Profitability (%)					
ROE	11.7%	8.6%	6.6%	7.2%	8.8%
ROIC	18.6%	7.8%	7.0%	10.2%	14.9%
Per share data (RMB)					
EPS (RMB)	0.30	0.22	0.20	0.28	0.37
DPS (RMB)	0.20	0.20	0.00	0.00	0.00
BVPS (RMB)	2.61	2.42	3.76	4.03	4.41

Source: Company data, CMBIGM estimates

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