Shennan Circuit (002916 CH)

Soft 1H23 numbers suggest no immediate turnaround

The worldwide PCB market experienced a significant decline of 20% YoY in 1H23, mainly due to falling demand for electronics products under global macroeconomic pressure. This is in line with our previous prediction that *"we expect the global PCB market will persistently encounter macroeconomic challenges due to weakened consumer demand and the ongoing destocking cycle among downstream industries."* (link) **Shennan Circuit (002916 CH), a pure PCB manufacturer, is not immune to the market weakness. Maintain HOLD, with lowered TP of RMB72.**

- **PCB segment (nearly 2/3 of total revenue) remains weak, with margin erosion in a declining market.** Segment revenue dropped by 12.4% YoY and 11.6% QoQ to RMB3.9bn in 1H23. The gross margin declined by 1.49ppts to 25.9% compared to 1H22. Weakening demand in domestic and overseas telecom markets and delay in upgrade for Eagle stream platform dragged the segment sales. The contribution of the Company's AI server related PCB products was not meaningful, suggesting Shennan is not yet a key beneficiary from the current AI boom. Auto PCB was the only spotlight, with 40% YoY growth in orders due to a low base.
- **Substrate segment was dealt a heavy blow with a significant 39.9% YoY drop in revenue, as downstream manufacturers continued destocking.** Although the Company actively ventured into new projects and cultivated new customer relationships, ASP erosion was particularly severe for package substrate. GPM was 18.8% in 1H23 vs. 30.3% and 23.1% in 1H22/2H22, affected by market down cycle and rising costs of new factories.
- The Company reported a 13.5% YoY decline in revenue to RMB6.0bn and a substantial 37.02% YoY drop in net profit to RMB474mn in 1H23. GPM was lowered to 22.9% vs. 26.5% and 24.6% in 1H22/2H22. The Company's 1H23 results were below our estimates, which were already lower than consensus. We cut FY23/24E revenue and NP by 14%/14% and 29%/24%, as we think the business will continue to be affected by industry downcycle and a near-term turnaround may not be imminent. **Maintain HOLD, with lowered TP of RMB72, based on 25x rollover 2024E P/E.** We keep the same P/E multiple of 25x, which is over 1SD below 5-year historical avg., as the market is waiting for a clear sign of demand recovery.

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	13,943	13,992	12,693	14,672	17,490
YoY growth (%)	20.2	0.4	(9.3)	15.6	19.2
Gross margin (%)	23.7	25.5	23.1	24.0	25.3
Net profit (RMB mn)	1,481	1,640	1,098	1,480	2,088
YoY growth (%)	3.5	10.7	(33.0)	34.8	41.0
EPS (Reported) (RMB)	3.02	3.22	2.13	2.88	4.06
P/E (x)	33.6	28.3	30.8	22.8	16.2
ROE (%)	18.6	15.8	8.8	11.1	14.2

Source: Company data, Bloomberg, CMBIGM estimates

HOLD (Maintain)

Target Price	**RMB72.00**
(Previous TP	RMB96.60)
Up/Downside	**9.7%**
Current Price	**RMB65.66**

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Stock Data

Mkt Cap (RMB mn)	33,677.0
Avg 3 mths t/o (RMB mn)	216.0
52w High/Low (RMB)	98.86/62.14
Total Issued Shares (mn)	512.9

Source: FactSet

Shareholding Structure

AVIC International Holdings Ltd	64.0%
HKSCC	3.1%

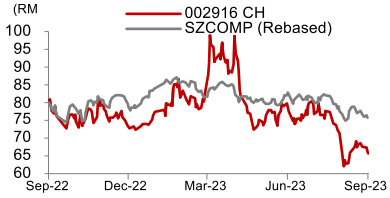
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-8.0%	-5.3%
3-mth	-17.4%	-9.1%
6-mth	-24.1%	-17.6%

Source: FactSet

12-mth Price Performance



Source: FactSet

Figure 1: CMBIGM estimates vs. consensus

	CMBI estimates			Consensus			Diff (%)		
RMB mn	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	12,693	14,672	17,490	14,816	17,121	19,497	-14%	-14%	-10%
Gross Profit	2,930	3,521	4,419	3,546	4,234	4,905	-17%	-17%	-10%
Operating Profit	1,103	1,554	2,190	1,657	2,081	2,457	-33%	-25%	-11%
Net profit	1,098	1,480	2,088	1,540	1,940	2,267	-29%	-24%	-8%
EPS (RMB)	2.13	2.88	4.06	3.19	3.85	4.45	-33%	-25%	-9%
Gross Margin	23.1%	24.0%	25.3%	23.9%	24.7%	25.2%	-0.8 ppt	-0.7 ppt	0.1 ppt
Operating Margin	8.7%	10.6%	12.5%	11.2%	12.2%	12.6%	-2.5 ppt	-1.6 ppt	-0.1 ppt
Net Margin	8.7%	10.1%	11.9%	10.4%	11.3%	11.6%	-1.7 ppt	-1.2 ppt	0.3 ppt

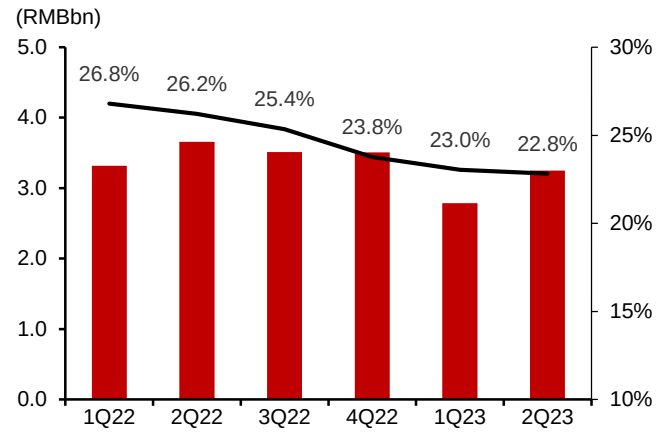
Source: Company data, CMBIGM estimates

Figure 2: Earnings revision

	New			Old			Diff (%)		
RMB mn	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	12,693	14,672	17,490	15,108	17,475	NA	-16%	-16%	NA
Gross Profit	2,930	3,521	4,419	3,944	4,587	NA	-26%	-23%	NA
Operating Profit	1,103	1,554	2,190	1,879	2,195	NA	-41%	-29%	NA
Net profit	1,098	1,480	2,088	1,723	2,014	NA	-36%	-26%	NA
EPS (RMB)	2.13	2.88	4.06	3.52	4.12	NA	-39%	-30%	NA
Gross Margin	23.1%	24.0%	25.3%	26.1%	26.2%	NA	-3 ppt	-2.3 ppt	NA
Operating Margin	8.7%	10.6%	12.5%	12.4%	12.6%	NA	-3.7 ppt	-2 ppt	NA
Net Margin	8.7%	10.1%	11.9%	11.4%	11.5%	NA	-2.8 ppt	-1.4 ppt	NA

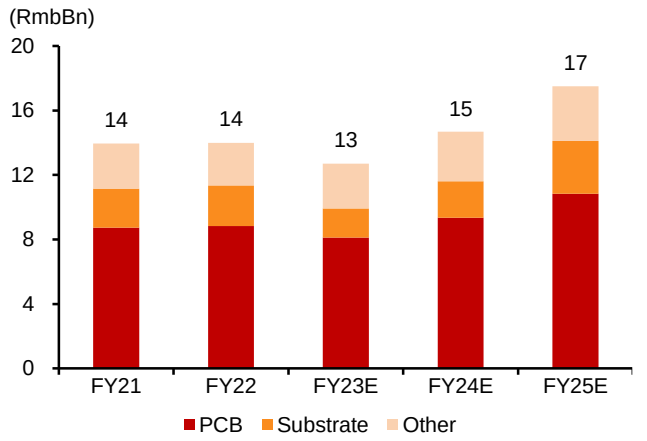
Source: Company data, CMBIGM estimates

Figure 3: Company's soft 1H23 results suggest no immediate turnaround (1Q22-2Q23)



Source: Company data, CMBIGM estimates

Figure 4: Company's revenue breakdown by segments



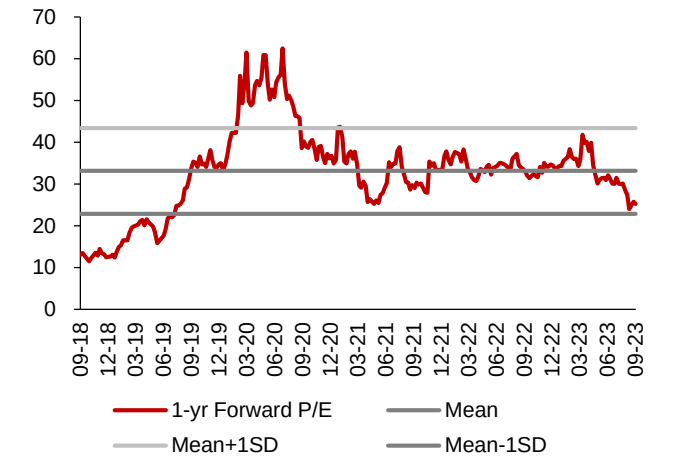
Source: Company data, CMBIGM estimates

Figure 5: Revenue forecast breakdown

RMB mn	FY20E	FY21E	FY22E	1H23	2H23E	FY23E	FY24E	FY25E
PCB	8,311	8,737	8,825	3,882	4,244	8,125	9,352	10,844
…YoY	*7.6%*	*5.1%*	*1.0%*	*-12.4%*	*-3.4%*	*-7.9%*	*15.1%*	*16.0%*
…%	*72%*	*63%*	*63%*	*64%*	*64%*	*64%*	*64%*	*62%*
Substrate	1,544	2,415	2,520	821	971	1,792	2,252	3,265
…YoY	*32.7%*	*56.3%*	*4.4%*	*-39.9%*	*-15.8%*	*-28.9%*	*25.7%*	*45.0%*
…%	*13%*	*17%*	*18%*	*14%*	*15%*	*14%*	*15%*	*19%*
PCBA	1,160	1,940	1,744	850	931	1,782	1,975	2,177
…YoY	*-4.2%*	*67.2%*	*-10.1%*	*20.3%*	*-10.2%*	*2.1%*	*10.8%*	*10.3%*
…%	*10%*	*14%*	*12%*	*14%*	*14%*	*14%*	*13%*	*12%*
Other	585	851	904	480	513	994	1,093	1,203
…YoY	*38.4%*	*45.4%*	*6.2%*	*3.1%*	*17.3%*	*10.0%*	*10.0%*	*10.0%*
…%	*5%*	*6%*	*6%*	*8%*	*8%*	*8%*	*7%*	*7%*
Total	**11,600**	**13,943**	**13,992**	**6,034**	**6,660**	**12,693**	**14,672**	**17,490**
…YoY	**10.2%**	**20.2%**	**0.4%**	**-11.1%**	**-3.7%**	**-9.3%**	**15.6%**	**19.2%**

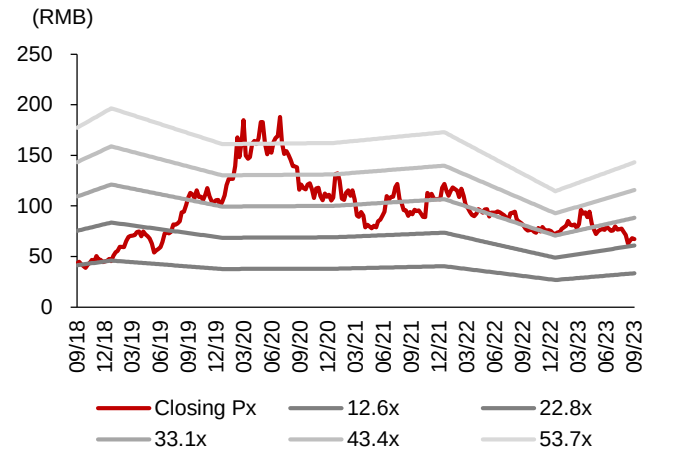
Source: Company data, CMBIGM estimates

Figure 6: 12M forward PE band



Source: Company data, CMBIGM estimates

Figure 7: 12M forward PE chart



Source: Company data, CMBIGM estimates

Financial Summary

INCOME STATEMENT	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Revenue	**11,600**	**13,943**	**13,992**	**12,693**	**14,672**	**17,490**
Cost of goods sold	(8,530)	(10,637)	(10,422)	(9,763)	(11,152)	(13,070)
Gross profit	**3,071**	**3,306**	**3,571**	**2,930**	**3,521**	**4,419**
Operating expenses	**(1,174)**	**(1,406)**	**(1,691)**	**(1,605)**	**(1,774)**	**(2,059)**
Selling expense	(231)	(319)	(340)	(373)	(394)	(492)
Admin expense	(480)	(543)	(673)	(571)	(646)	(752)
R&D expense	(645)	(782)	(820)	(790)	(884)	(992)
Others	182	238	142	129	149	177
Operating profit	**1,625**	**1,617**	**1,723**	**1,103**	**1,554**	**2,190**
Other income	8	4	4	6	6	8
Other expense	(27)	(11)	(7)	(4)	(6)	(7)
Pre-tax profit	**1,606**	**1,609**	**1,720**	**1,105**	**1,553**	**2,191**
Income tax	(175)	(128)	(80)	(7)	(73)	(102)
After tax profit	**1,431**	**1,481**	**1,640**	**1,098**	**1,481**	**2,088**
Minority interest	1	0	0	0	0	0
Net profit	**1,430**	**1,481**	**1,640**	**1,098**	**1,480**	**2,088**
Gross dividends	465	499	513	343	463	653

BALANCE SHEET	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Current assets	**5,941**	**7,270**	**8,578**	**7,682**	**8,527**	**9,922**
Cash & equivalents	504	620	1,912	675	909	1,462
Restricted cash	2	0	1	1	1	1
Account receivables	2,799	3,895	3,805	3,541	3,877	4,394
Inventories	2,206	2,527	2,341	2,474	2,720	3,009
Prepayment	6	16	49	28	33	40
Financial assets at FVTPL	165	0	271	700	700	700
Other current assets	258	213	199	262	286	314
Non-current assets	**8,067**	**9,522**	**12,149**	**13,271**	**14,328**	**15,231**
PP&E	6,485	7,789	9,138	9,937	10,625	11,303
Right-of-use assets	0	44	37	30	24	18
Deferred income tax	72	91	208	272	297	326
Investment in JVs & assos	6	6	6	6	6	7
Intangibles	322	407	557	537	518	500
Goodwill	0	0	0	0	0	0
Financial assets at FVTPL	118	121	65	65	65	65
Other non-current assets	1,064	1,064	2,138	2,425	2,793	3,012
Current liabilities	**4,932**	**5,948**	**6,708**	**5,836**	**6,389**	**6,857**
Short-term borrowings	232	350	0	420	668	758
Account payables	3,772	4,438	4,632	4,524	4,788	5,088
Tax payable	22	78	31	86	94	104
Other current liabilities	467	583	1,491	365	367	370
Contract liabilities	97	70	93	98	100	127
Accrued expenses	342	428	462	342	373	411
Non-current liabilities	**1,066**	**1,725**	**1,384**	**1,891**	**2,064**	**2,224**
Long-term borrowings	1,059	1,368	1,175	1,720	1,877	2,018
Bond payables	0	0	0	0	0	0
Deferred income	6	7	209	171	187	206
Other non-current liabilities	0	350	0	0	0	0
Total liabilities	**5,998**	**7,672**	**8,092**	**7,727**	**8,454**	**9,080**
Share capital	489	489	513	511	511	511
Capital surplus	0	0	0	0	0	0
Retained earnings	3,135	4,150	5,291	5,868	6,995	8,605
Other reserves	3,783	3,844	6,410	6,416	6,427	6,442
Total shareholders equity	**7,407**	**8,484**	**12,214**	**12,796**	**13,933**	**15,558**
Minority interest	3	3	3	4	4	4
Total equity and liabilities	**13,408**	**16,159**	**20,309**	**20,527**	**22,390**	**24,643**

CASH FLOW	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	**1,431**	**1,481**	**1,640**	**1,098**	**1,481**	**2,088**
Depreciation & amortization	644	863	1,079	1,203	1,353	1,508
Tax paid	1	(18)	85	(102)	(9)	(11)
Change in working capital	(558)	(344)	95	(209)	(217)	(318)
Others	282	361	281	180	(20)	(70)
Net cash from operations	**1,800**	**2,342**	**3,180**	**2,170**	**2,588**	**3,197**
Investing						
Capital expenditure	(2,486)	(2,658)	(3,378)	(2,480)	(2,363)	(2,351)
Acquisition of subsidiaries/ investments	6	2	6	(414)	19	19
Net proceeds from disposal of short-term investments	1,858	1,818	5,146	(0)	0	(0)
Others	(2,013)	(1,642)	(5,388)	(0)	(1)	(1)
Net cash from investing	**(2,635)**	**(2,481)**	**(3,614)**	**(2,893)**	**(2,345)**	**(2,332)**
Financing						
Dividend paid	(453)	(541)	(565)	(580)	(414)	(542)
Net borrowings	87	536	(242)	(169)	405	231
Proceeds from share issues	0	0	2,530	(3)	0	0
Others	(9)	(34)	(34)	211	(27)	(27)
Net cash from financing	**(375)**	**(40)**	**1,689**	**(541)**	**(36)**	**(338)**
Net change in cash						
Cash at the beginning of the year	1,441	504	620	1,912	675	909
Exchange difference	(31)	(7)	30	30	30	30
Others	(905)	122	1,263	(1,267)	204	524
Cash at the end of the year	**504**	**620**	**1,912**	**675**	**909**	**1,462**

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