

Shennan Circuits (002916 CH)

Pending industry recovery with in-line 3Q results

Shennan Circuits released its 3Q results. Revenue was RMB3.4bn, with YoY growth of -2.4% and QoQ growth of 5.5%. Net profit (NP) was RMB434mn, with YoY growth of 1.1% and QoQ growth of 62.3% (including a one-time government subsidy of RMB151mn). Gross margin slightly expanded to 23.4% in 3Q from 23.0% and 22.8% in 1Q and 2Q, driven by 1) a favorable product mix, 2) cost optimization, and 3) improved utilization in the substrate segment. We think QoQ growth in revenue and margin improvement are positive signs, suggesting the industry is bottoming out gradually. **We maintain HOLD on Shennan Circuits with an adjusted TP of RMB73.2**, considering weak demand from legacy telecom spending and the ongoing macro pressure.

- **Shennan's 3Q revenue grew 5.5% QoQ, in line with our estimate.** The mild growth was largely driven by customer restocking. We believe 4Q revenue should remain at a similar level, as we do not expect a meaningful rise in demand in the near term. We estimate overall revenue to decline 8.1% YoY in 2023. For 2024/25E, we expect revenue to grow 14.3% and 18.2% YoY.
- **For PCB segment**, 1) auto products continued to serve as a primary revenue driver, 2) telecom demand remained weak, and 3) modest revenue growth was seen in the Datacom market. **For substrate segment**, sales of substrate products in 3Q were better than 1H23, with an improving utilization rate. We start to see recovering signs in the semi industry.
- **Maintain HOLD with adjusted TP of RMB73.2.** We adjust our 2023/24/25E NP by 15%/2%/-3%. We revise up 2023 NP estimate, mainly due to the one-time government subsidy. Our new TP is RMB73.2 based on the same multiple of 25x 2024E P/E, slightly higher than 1SD below 5-year historical average. We think the valuation is justified given the PCB sector is still facing challenges and weak telecom demand for legacy products.

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Turnover (RMB mn)	13,943	13,992	12,859	14,692	17,371
YoY growth (%)	20.2%	0.4%	-8.1%	14.3%	18.2%
Gross margin (%)	23.7%	25.5%	23.4%	24.3%	25.4%
Net profit (RMB mn)	1,481	1,640	1,255	1,506	2,030
YoY growth (%)	3.5%	10.7%	-23.5%	20.0%	34.8%
EPS (RMB)	3.0	3.2	2.4	2.9	3.9
Consensus EPS (RMB)	NA	NA	3.3	3.9	4.4
P/E (x)	22.7	21.3	28.1	23.5	17.4
ROE (%)	17.4%	13.4%	9.7%	10.7%	13.0%

Source: Company data, Bloomberg, CMBIGM estimates

HOLD (Maintain)

Target Price **RMB73.20**
 (Previous TP RMB72.00)
Up/Downside **6.6%**
Current Price **RMB68.68**

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Stock Data

Mkt Cap (RMB mn)	35,226.0
Avg 3 mths t/o (RMB mn)	180.0
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%

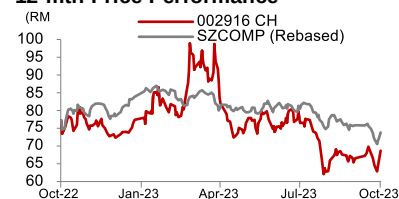
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	5.2%	7.7%
3-mth	-10.2%	-2.1%
6-mth	-16.2%	-8.6%

Source: FactSet

12-mth Price Performance



Source: FactSet

Figure 1: CMBIGM estimates vs. consensus

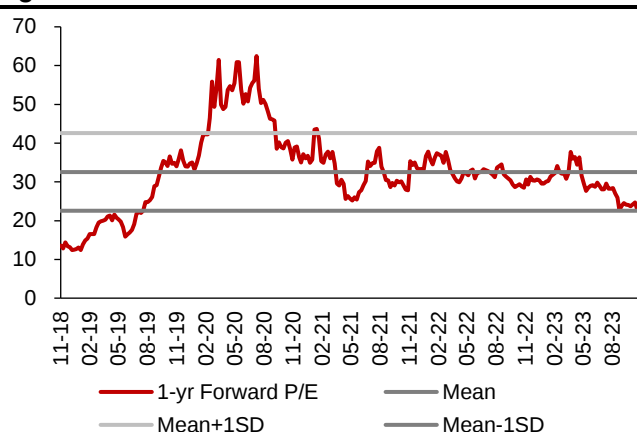
RMB mn	CMBI estimates			Consensus			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	12,859	14,692	17,371	14,211	16,926	19,324	-10%	-13%	-10%
Gross profit	3,009	3,569	4,409	3,384	4,171	4,864	-11%	-14%	-9%
Net profit	1,255	1,506	2,030	1,459	1,962	2,302	-14%	-23%	-12%
EPS (RMB)	2.44	2.93	3.95	3.25	3.88	4.44	-25%	-24%	-11%
Gross margin	23.4%	24.3%	25.4%	23.8%	24.6%	25.2%	-0.4 ppt	-0.3 ppt	0.2 ppt
Net margin	9.6%	10.8%	12.3%	10.7%	12.1%	12.7%	-1.1 ppt	-1.3 ppt	-0.5 ppt

Source: Company data, CMBIGM estimates

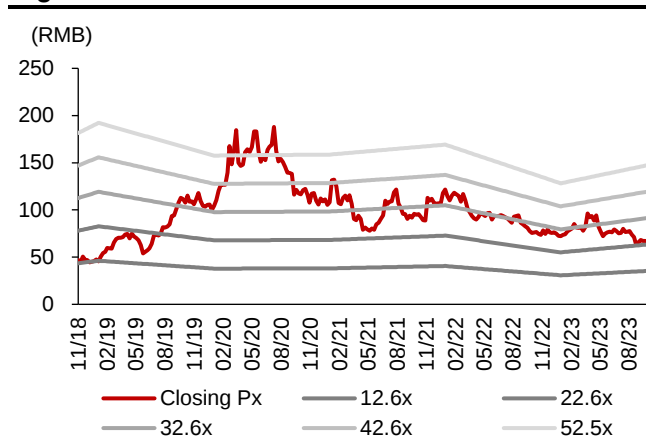
Figure 2: Earnings revision

RMB mn	New			Old			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	12,859	14,692	17,371	12,693	14,672	17,490	1%	0%	-1%
Gross profit	3,009	3,569	4,409	2,930	3,521	4,419	3%	1%	0%
Net profit	1,255	1,506	2,030	1,098	1,480	2,088	14%	2%	-3%
EPS (RMB)	2.44	2.93	3.95	2.13	2.88	4.06	15%	2%	-3%
Gross margin	23.4%	24.3%	25.4%	23.1%	24.0%	25.3%	0.3 ppt	0.3 ppt	0.1 ppt
Net margin	9.6%	10.8%	12.3%	8.7%	10.6%	12.5%	0.9 ppt	0.2 ppt	-0.3 ppt

Source: Company data, CMBIGM estimates

Figure 1: 12M forward PE band

Source: Company data, CMBIGM estimates

Figure 2: 12M forward PE chart

Source: Company data, CMBIGM estimates

Figure 5: P&L summary

RMB mn	FY21	FY22	1Q23	2Q23	3Q23	4Q23E	FY23E	FY24E	FY25E
Revenue	13,943	13,992	2,785	3,249	3,428	3,397	12,859	14,692	17,371
YoY	20.2%	0.4%	-16.0%	-11.1%	-2.4%	-3.1%	-8.1%	14.3%	18.2%
QoQ			-20.6%	16.7%	5.5%	-0.9%			
Seasonality			21.7%	25.3%	26.7%	26.4%			
Cost of sales	(10,637)	(10,422)	(2,039)	(7,732)	(1,858)	(2,507)	(9,850)	(11,123)	(12,962)
Gross profit	3,306	3,571	642	742	803	822	3,009	3,569	4,409
YoY	7.6%	8.0%	-27.7%	-22.6%	-9.8%	-1.4%	-15.7%	18.6%	23.5%
GPM (%)	23.7%	25.5%	23.0%	22.8%	23.4%	24.2%	23.4%	24.3%	25.4%
SG&A	(776)	(926)	(189)	(229)	(206)	(227)	(852)	(959)	(1,099)
% of revenue	(5.6%)	(6.6%)	(6.8%)	(7.1%)	(6.0%)	(6.7%)	(6.6%)	(6.5%)	(6.3%)
R&D	(782)	(820)	(166)	(211)	(259)	(221)	(857)	(979)	(1,140)
% of revenue	(5.6%)	-5.9%	-6.0%	-6.5%	-7.5%	-6.5%	-6.7%	-6.7%	-6.6%
Other expenses	(130)	(102)	(77)	(62)	100	(23)	(63)	(51)	(41)
% of revenue	(0.9%)	(0.7%)	(2.8%)	(1.9%)	2.9%	(0.7%)	(0.5%)	(0.3%)	(0.2%)
Net profit	1,481	1,640	206	268	434	347	1,255	1,506	2,030
YoY	3.5%	10.7%	-40.7%	-33.8%	1.1%	-24.2%	-23.5%	20.0%	34.8%
QoQ			-4.2%	29.6%	62.3%	-20.1%			
NPM (%)	10.6%	11.7%	7.4%	8.2%	12.7%	10.2%	9.8%	10.3%	11.7%

Financial Summary

INCOME STATEMENT	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Revenue	11,600	13,943	13,992	12,859	14,692	17,371
Cost of goods sold	(8,530)	(10,637)	(10,422)	(9,850)	(11,119)	(12,957)
Gross profit	3,071	3,306	3,571	3,009	3,573	4,414
Operating expenses	(1,174)	(1,406)	(1,691)	(1,532)	(1,748)	(2,015)
SG&A expense	(647)	(776)	(926)	(852)	(929)	(1,098)
R&D expense	(645)	(782)	(820)	(857)	(950)	(1,062)
Others	117	152	55	177	130	145
Operating profit	1,897	1,899	1,880	1,477	1,825	2,399
Other income	8	4	4	5	5	7
Other expense	(27)	(11)	(7)	(3)	(5)	(6)
Other gains/(losses)	(120)	(175)	(163)	(221)	(180)	(214)
Interest income	10	5	22	12	6	10
Interest expense	(113)	(91)	(92)	(78)	(89)	(89)
Others	(49)	(21)	77	47	67	79
Pre-tax profit	1,606	1,609	1,720	1,238	1,628	2,187
Income tax	(175)	(128)	(80)	17	(76)	(102)
After tax profit	1,431	1,481	1,640	1,255	1,552	2,084
Minority interest	1	0	0	0	0	0
Net profit	1,430	1,481	1,640	1,255	1,551	2,084

BALANCE SHEET	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Current assets	5,941	7,270	8,578	7,732	8,313	9,173
Cash & equivalents	507	620	1,913	472	711	1,359
Account receivables	2,053	2,732	2,770	3,078	3,201	3,271
Inventories	2,206	2,527	2,341	2,733	2,873	2,949
Prepayment	6	16	49	29	33	39
Other current assets	1,169	1,377	1,505	1,421	1,494	1,555
Non-current assets	8,067	9,522	12,149	14,060	14,900	15,762
PP&E	6,485	7,789	9,138	9,954	10,564	11,172
Right-of-use assets	0	44	37	30	24	18
Deferred income tax	72	91	208	280	298	320
Intangibles	322	407	557	537	518	500
Goodwill	0	0	0	0	0	0
Other non-current assets	1,188	1,191	2,209	3,258	3,495	3,752
Total assets	14,008	16,792	20,727	21,792	23,212	24,936
Current liabilities	4,932	5,948	6,708	5,789	6,087	6,353
Short-term borrowings	232	350	0	524	708	765
Account payables	1,515	1,881	1,638	1,816	1,840	1,923
Tax payable	22	78	31	86	91	98
Other current liabilities	2,724	3,141	4,484	2,772	2,870	2,936
Contract liabilities	97	70	93	193	153	174
Accrued expenses	342	428	462	399	425	456
Non-current liabilities	1,631	2,325	1,765	3,008	2,969	2,824
Long-term borrowings	1,059	1,368	1,175	2,477	2,403	2,216
Bond payables	0	0	0	0	0	0
Deferred income	6	7	209	169	180	193
Other non-current liabilities	566	950	382	363	386	415
Total liabilities	6,563	8,272	8,474	8,797	9,055	9,177
Share capital	489	489	513	511	511	511
Retained earnings	3,135	4,150	5,291	6,024	7,172	8,756
Other reserves	3,817	3,877	6,446	6,456	6,470	6,487
Total shareholders equity	7,441	8,517	12,249	12,992	14,153	15,755
Minority interest	3	3	3	4	4	4
Total equity and liabilities	14,008	16,792	20,727	21,792	23,212	24,936

CASH FLOW	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	1,431	1,481	1,640	1,255	1,552	2,084
Depreciation & amortization	644	863	1,079	1,220	1,359	1,509
Change in working capital	(557)	(363)	180	(984)	(58)	103
Others	282	361	281	196	(84)	(24)
Net cash from operations	1,800	2,342	3,180	1,688	2,769	3,672
Investing						
Capital expenditure	(2,486)	(2,658)	(3,378)	(3,350)	(2,177)	(2,341)
Acquisition of subsidiaries/ investments	0	(3)	0	0	0	0
Net proceeds from disposal of short-term investments	0	0	0	0	0	0
Others	(149)	181	(237)	14	17	18
Net cash from investing	(2,635)	(2,481)	(3,614)	(3,336)	(2,159)	(2,323)
Financing						
Dividend paid	(453)	(541)	(565)	(591)	(482)	(574)
Net borrowings	87	536	(242)	692	110	(130)
Proceeds from share issues	0	0	2,530	(3)	0	0
Others	295	266	(26)	211	(27)	(27)
Net cash from financing	(71)	261	1,697	308	(398)	(731)
Net change in cash						
Cash at the beginning of the year	1,441	504	620	1,912	471	710
Exchange difference	(31)	(7)	30	30	30	30
Others	(905)	122	1,263	(1,471)	209	617
Cash at the end of the year	504	620	1,912	471	710	1,357

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