19 Aug 2024

CMB International Global Markets | Equity Research | Company Update

Kingdee (268 HK)

Macro headwinds weighed on growth; loss reduction on track

Kingdee reported its 1H24 results: revenue was up 11.9% YoY (1H23: 16.8% YoY) to RMB2.87bn, 2% shy of Bloomberg consensus, which in our view can be attributed to a lengthened deal cycle and softer-than-expected growth amid macro headwinds (especially small and micro enterprises, whose YoY revenue growth slowed to 9% YoY in 1H24 from 19% in 1H23), while the net loss of RMB218mn implies a YoY reduction of 23% and was 20% narrower than consensus estimates, which demonstrated Kingdee's determination to improve operating efficiency. Core SaaS product Galaxy's ARR growth momentum remained healthy with 24% YoY growth in subscription ARR in 1H24 (1H23: +29% YoY). Meanwhile, large enterprise revenue growth of 38.9% YoY (1H23: 38.4%) remains solid, in our view. Although we still expect the demand recovery to take time, especially for small enterprises, we are expecting the second half to deliver results driven by healthy growth in Kingdee's contract value and the lengthened deal cycle. We lower 2024E revenue forecast by 4%, but expect 2H24 revenue growth to reaccelerate to 16%. We maintain BUY rating but lower target price to HK$10.8 per share (was HK$15.5), based on 4.4x 2024E EV/Sales (was 6.4x), in line with the one year mean.

- **Revenue contribution from cloud continued rising.** In 1H24, cloud revenue grew 17.2% YoY to RMB2.4bn, and was 83.2% of total revenue (1H23: 79.5%), while license ERP revenue declined by -8.8% YoY. Net loss shrank to RMB218mn in 1H24 (1H23: RMB284mn), driven by GPM expansion (+1.3pp YoY to 63.2% in 1H24) aided by an increase in cloud revenue contribution. The continuously rising trend in cloud revenue contribution should help enhance operating efficiency, in our view.
- **Galaxy sustained healthy revenue growth and healthy profitability.** In 1H24, Kingdee's core SaaS product Galaxy achieved revenue of RMB1.1bn, up 14.3% YoY (1H23: 17.3%), and Galaxy's subscription ARR was up 24% YoY (1H23: 29%). Dollar retention rate edged down to 95% in 1H24 from 96% in 1H23 due to macro headwinds. Customer acquisition for Galaxy was on track, in our view, with c.8,000 YoY net adds in 1H24, and the profitability of Galaxy remained healthy at c.20%.
- **Large enterprises: solid revenue growth contribution although facing a longer deal cycle.** Benefiting from ongoing software localization demand, as well as enhanced product capability, Kingdee Cosmic & Constellation (C&C) revenue grew 38.9% YoY in 1H24 (1H23: 38.4% YoY) to RMB546mn (19% of revenue, as compared to 15% in 1H23). Kingdee signed up 275 new customers for C&C business during 1H24. Management highlighted a solid expansion trajectory for life time contract value (LTCV) of C&C customers from the initial contracts: in 1H24, the LTCV expanded to 5.3x/3.8x/2.9x/1.9x/1.8x/1.2x of initial value for the contracts signed in 2018/2019/2020/2021/2022/2023.
- **Guidance on OCF growth and breakeven point remains unchanged driven by efficiency improvement.** Management's guidance on continued loss reduction and breakeven in 2025 remains unchanged. Although the overall pace of revenue growth is likely to be slightly slower than our previous expectation, but management's guidance on OCF of RMB900mn for 2024 remains unchanged as it is confident in driving operating efficiency improvement.

BUY (Maintain)

Target Price	**HK$10.80**
(Previous TP	HK$15.50)
Up/Downside	**84.9%**
Current Price	**HK$5.84**

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Stock Data

Mkt Cap (HK$ mn)	20,294.0
Avg 3 mths t/o (HK$ mn)	116.6
52w High/Low (HK$)	13.04/5.56
Total Issued Shares (mn)	3475.0

Source: FactSet

Shareholding Structure

Mr. Xu - Chairman	20.3%
Oriental Tao Limited	11.1%

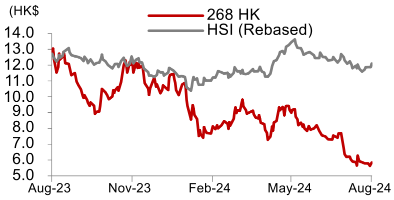
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-8.3%	-6.8%
3-mth	-35.0%	-27.8%
6-mth	-28.2%	-33.4%

Source: FactSet

12-mth Price Performance



Source: FactSet

Earnings Summary

(YE 31 Dec)	FY22A	FY23A	FY24E	FY25E	FY26E
Revenue (RMB mn)	4,866	5,679	6,475	7,682	8,902
YoY growth (%)	16.6	16.7	14.0	18.6	15.9
Net profit (RMB mn)	(389.2)	(209.9)	(11.5)	240.6	466.8
EPS (Reported) (RMB cents)	(11.21)	(6.04)	(0.33)	6.92	13.44
Consensus EPS (RMB cents)	na	na	(1.40)	6.87	15.90
P/E (x)	ns	ns	ns	77.6	40.0

Source: Company data, Bloomberg, CMBIGM estimates

Figure 1: Kingdee: change in CMBI forecast

	2024E			2025E			2026E		
RMBmn	New	Old	%Diff	New	Old	%Diff	New	Old	%Diff
Sales	6,475	6,722	-4%	7,682	7,980	-4%	8,902	9,250	-4%
Gross profit	4,201	4,335	-3%	5,008	5,172	-3%	5,833	6,025	-3%
Operating profit	-393	-405	-3%	-70	-80	-12%	199	199	-0%
PBT	-67	-78	-14%	238	246	-3%	504	521	-3%
Net profit	-11	-11	9%	240	252	-5%	466	484	-4%
EPS	-0.00	-0.00	9%	0.07	0.07	-5%	0.13	0.14	-4%
Margins									
GM	64.9%	64.5%	40 bps	65.2%	64.8%	38 bps	65.5%	65.1%	38 bps
OPM	-6.1%	-6.0%	-5 bps	-0.9%	-1.0%	8 bps	2.2%	2.2%	8 bps
PBT margin	-1.0%	-1.2%	13 bps	3.1%	3.1%	2 bps	5.7%	5.6%	2 bps
Net margin	-0.2%	-0.2%	-2 bps	3.1%	3.2%	-3 bps	5.2%	5.2%	0 bps

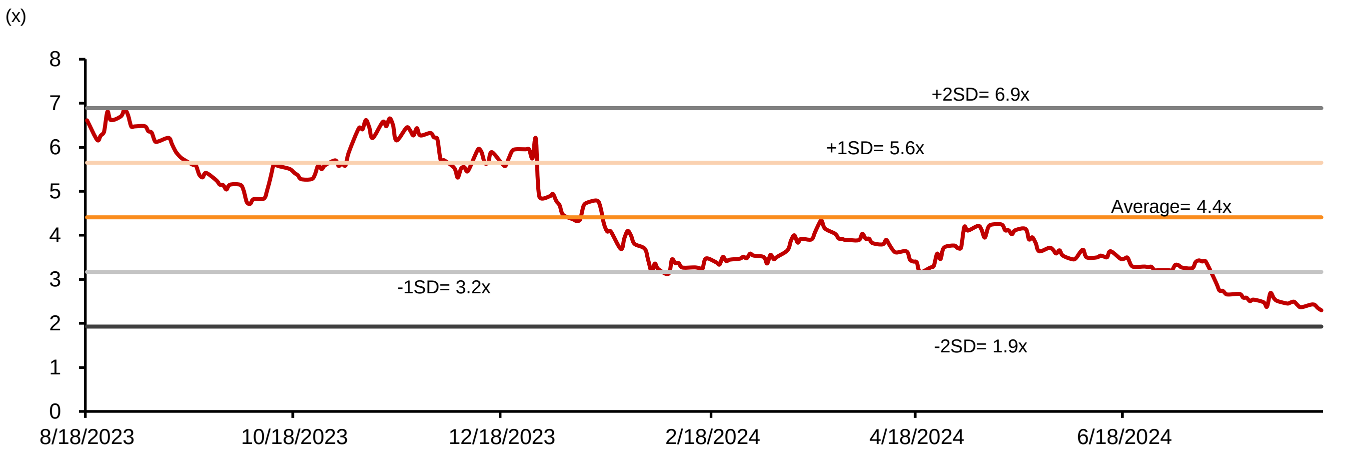
Source: CMBIGM estimates

Figure 2: Kingdee: CMBI forecast vs Bloomberg consensus

	2024			2025			2026		
RMBm	CMBI	Street	Diff	CMBI	Street	Diff	CMBI	Street	Diff
Sales	6,475	6,598	-2%	7,682	7,749	-1%	8,902	9,075	-2%
Gross profit	4,201	4,306	-2%	5,008	5,117	-2%	5,833	6,101	-4%
Operating profit	-393	-203	93%	-70	160	-144%	199	460	-57%
Profit before tax	-67	-74	-9%	238	272	-12%	504	618	-18%
Net profit	-11	-58	-80%	240	219	9%	466	540	-14%
EPS	-0.00	-0.08	-96%	0.07	-0.08	-191%	0.13	0.92	-85%
Margins									
GM	64.9%	65.3%	-36 bps	65.2%	66.0%	-84 bps	65.5%	67.2%	-171 bps
OPM	-6.1%	-3.1%	-299 bps	-0.9%	2.1%	-298 bps	2.2%	5.1%	-283 bps
Profit before tax margin	-1.0%	-1.1%	8 bps	3.1%	3.5%	-41 bps	5.7%	6.8%	-115 bps
Net margin	-0.2%	-0.9%	70 bps	3.1%	2.8%	29 bps	5.2%	5.9%	-71 bps

Source: Bloomberg, CMBIGM estimates

Figure 3: Kingdee: one-year average EV/Sales



Source: Bloomberg, CMBIGM estimates

Risks

1) Slower-than-expected revenue growth; 2) slower-than-expected margin expansion; 3) more intensified-than-expected industry competition.

Financial Summary

INCOME STATEMENT	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Dec (RMB mn)						
Revenue	**4,174**	**4,866**	**5,679**	**6,475**	**7,682**	**8,902**
Cost of goods sold	(1,541)	(1,868)	(2,035)	(2,273)	(2,674)	(3,069)
Gross profit	**2,634**	**2,998**	**3,644**	**4,201**	**5,008**	**5,833**
Operating expenses	**(3,392)**	**(3,826)**	**(4,249)**	**(4,594)**	**(5,078)**	**(5,634)**
Selling expense	(1,741)	(2,027)	(2,320)	(2,524)	(2,800)	(3,106)
Admin expense	(466)	(504)	(490)	(532)	(571)	(648)
R&D expense	(1,185)	(1,295)	(1,440)	(1,539)	(1,707)	(1,879)
Operating profit	**(758)**	**(828)**	**(605)**	**(393)**	**(70)**	**199**
Net Interest income/(expense)	**76**	**100**	**90**	**89**	**80**	**91**
Others	299	254	214	237	229	215
Pre-tax profit	**(382)**	**(474)**	**(301)**	**(67)**	**239**	**505**
Income tax	44	22	31	5	(24)	(50)
Minority interest	36	63	60	51	25	13
Net profit	**(302)**	**(389)**	**(210)**	**(11)**	**241**	**467**

BALANCE SHEET	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Dec (RMB mn)						
Current assets	**4,471**	**3,984**	**5,703**	**5,503**	**5,866**	**6,431**
Cash & equivalents	2,047	1,943	2,964	2,766	3,042	3,525
Restricted cash	392	293	364	375	445	515
Prepayment	370	626	1,045	1,045	1,045	1,045
Other current assets	1,339	776	968	974	983	993
Contract assets	323	347	362	344	351	352
Non-current assets	**6,616**	**7,747**	**8,436**	**9,129**	**9,906**	**10,734**
PP&E	1,045	1,377	1,919	2,425	2,946	3,460
Intangibles	1,037	1,192	1,232	1,420	1,676	1,990
Other non-current assets	4,534	5,178	5,284	5,284	5,284	5,284
Total assets	**11,087**	**11,731**	**14,139**	**14,633**	**15,772**	**17,165**
Current liabilities	**3,084**	**3,766**	**4,529**	**5,058**	**5,987**	**6,906**
Short-term borrowings	0	85	20	22	21	23
Account payables	759	899	1,231	1,208	1,350	1,472
Other current liabilities	160	150	101	101	101	101
Contract liabilities	2,165	2,631	3,177	3,727	4,515	5,310
Non-current liabilities	**200**	**558**	**908**	**935**	**929**	**949**
Long-term borrowings	0	385	757	784	778	798
Other non-current liabilities	200	173	151	151	151	151
Total liabilities	**3,284**	**4,324**	**5,437**	**5,993**	**6,916**	**7,855**
Share capital	83	84	87	87	87	87
Capital surplus	5,149	5,085	6,512	6,512	6,512	6,512
Retained earnings	1,619	1,230	1,020	1,009	1,250	1,716
Other reserves	744	867	979	979	979	979
Total shareholders equity	**7,596**	**7,265**	**8,599**	**8,588**	**8,828**	**9,295**
Minority interest	207	142	103	52	27	14
Total equity and liabilities	**11,087**	**11,731**	**14,139**	**14,633**	**15,772**	**17,165**

CASH FLOW	2021A	2022A	2023A	2024E	2025E	2026E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	**(382)**	**(474)**	**(301)**	**(67)**	**239**	**505**
Depreciation & amortization	439	414	499	550	621	703
Tax paid	44	22	31	5	(24)	(50)
Change in working capital	560	328	299	529	843	836
Others	0	85	126	(116)	(108)	(119)
Net cash from operations	**661**	**374**	**653**	**901**	**1,572**	**1,874**
Investing						
Capital expenditure	(772)	(888)	(897)	(1,243)	(1,398)	(1,531)
Others	(433)	101	(408)	116	108	119
Net cash from investing	**(1,205)**	**(787)**	**(1,305)**	**(1,127)**	**(1,290)**	**(1,412)**
Financing						
Dividend paid	0	0	0	0	0	0
Net borrowings	(120)	473	307	29	(6)	22
Proceeds from share issues	0	0	1,412	0	0	0
Others	(24)	(172)	(48)	0	0	0
Net cash from financing	**(144)**	**301**	**1,671**	**29**	**(6)**	**22**
Net change in cash						
Cash at the beginning of the year	2,754	2,047	1,943	2,964	2,766	3,042
Exchange difference	(19)	8	1	0	0	0
Cash at the end of the year	**2,047**	**1,943**	**2,964**	**2,766**	**3,042**	**3,525**
GROWTH	**2021A**	**2022A**	**2023A**	**2024E**	**2025E**	**2026E**
YE 31 Dec						
Revenue	24.4%	16.6%	16.7%	14.0%	18.6%	15.9%
Gross profit	19.2%	13.8%	21.6%	15.3%	19.2%	16.5%
Net profit	na	na	na	na	na	94.0%
PROFITABILITY	**2021A**	**2022A**	**2023A**	**2024E**	**2025E**	**2026E**
YE 31 Dec						
Gross profit margin	63.1%	61.6%	64.2%	64.9%	65.2%	65.5%
Operating margin	(18.2%)	(17.0%)	(10.7%)	(6.1%)	(0.9%)	2.2%
Return on equity (ROE)	(3.9%)	(5.2%)	(2.6%)	(0.1%)	2.8%	5.2%
GEARING/LIQUIDITY/ACTIVITIES	**2021A**	**2022A**	**2023A**	**2024E**	**2025E**	**2026E**
YE 31 Dec						
Net debt to equity (x)	(0.3)	(0.2)	(0.2)	(0.2)	(0.2)	(0.3)
Current ratio (x)	1.4	1.1	1.3	1.1	1.0	0.9
Receivable turnover days	31.7	25.7	21.1	21.1	21.1	21.1
Inventory turnover days	2.2	2.8	2.9	2.9	2.9	2.9
Payable turnover days	184.1	162.0	191.1	194.0	184.3	175.1
VALUATION	**2021A**	**2022A**	**2023A**	**2024E**	**2025E**	**2026E**
YE 31 Dec						
P/E	ns	ns	ns	ns	77.6	40.0
P/B	2.3	2.5	2.1	2.2	2.1	2.0
Div yield (%)	0.0	0.0	0.0	0.0	0.0	0.0
EV	(2,046.8)	(1,472.7)	(2,186.8)	(1,960.4)	(2,242.2)	(2,703.9)
EV/Sales	(0.5)	(0.3)	(0.4)	(0.3)	(0.3)	(0.3)

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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