

AAC Technologies (2018 HK)

Profit warning affirms our cautious view; Maintain Sell

AAC issued a profit warning for 1Q20, stating that its 1Q20 net profit will decline 85-90% YoY to Rmb 43mn-63mn, significantly below our/consensus estimates of Rmb 339mn/413mn, mainly due to 1) production suspension on CONV-19 outbreak, 2) seasonal pricing pressure, 3) weak smartphone demand, 4) higher expenses for work resumption arrangements. Despite normal production recovery since mid-March, AAC expects end demand will remain uncertain for rest of 2020, which echoes our cautious view on product launch delay, demand weakness and margin erosion ahead. We also expect no upgrade in haptics/acoustics for 2H20E iPhones. Our FY20/21E EPS are 32%/22% below consensus. Maintain Sell and lowered TP to HK\$ 29.0 based on 18x FY20E P/E.

- **1Q20 worse than feared on margin pressure and share loss.** In addition to less working days on CONV-19 impact, we believe AAC's 1Q20 miss was a result of 1) GPM erosion in acoustics/haptics, 2) share loss to Luxshare, and 3) casing ASP/margin pressure. In contrast to Luxshare's pre-announced 1Q with 55-60% YoY NP growth, AAC issued a profit warning with 85-90% YoY NP decline, which implies downside to market's positive view on AAC's stabilising haptics/acoustics market share and positive optics progress.
- **Optics remains too small to move the needle.** We think optics is the only bright spot for AAC, as mgmt. maintained bullish guidance to achieve 100kk/m plastic lens shipment by Jul 2020 (vs 45kk/m in 4Q19) and 6P/7P shipment will start in 3Q20E. While we are encouraged by AAC's optics positive progress, we think shipment/ASP guidance seems too aggressive given Sunny/Q-tech's conservative view and order uncertainty in 2H20E.
- **Our FY20/21E EPS are 32%/22% below consensus.** We trimmed our FY20-22E EPS by 4-19% to reflect higher margin pressure and continued demand weakness into 2H20E. We estimate net profit to grow -18%/-7%/+1% YoY in 2Q/3Q/4Q20E, driven by 1) more intense competition in acoustics/haptics, 2) slower optics ASP/shipment ramp, and 3) lack of major acoustics/haptics upgrade in 2H20 iPhone.
- **Maintain Sell and reduced TP to HK\$29.0 (31% downside).** We expect more earnings downside following 1Q20E miss and uncertainty of new iPhone launch timeline. Our new TP of HK\$29.0 is based on same target multiple of 18x FY20E P/E. Upside risks include stronger lens, better iPhone and less margin pressure.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	18,131	17,884	16,456	19,424	20,928
YoY growth (%)	(14.1)	(1.4)	(8.0)	18.0	7.7
Net income (RMB mn)	3,796	2,222	1,751	2,594	2,881
EPS (RMB)	3.12	1.84	1.45	2.14	2.38
YoY growth (%)	(28.5)	(41.1)	(21.2)	48.1	11.1
Consensus EPS (RMB)	NA	NA	2.14	2.70	3.09
P/E (x)	11.6	20.6	26.2	17.7	15.9
P/B (x)	2.3	2.3	2.3	2.1	1.9
Yield (%)	5.0	3.3	2.6	2.0	2.2
ROE (%)	20.0	11.3	8.7	11.9	12.1

Source: Company data, Bloomberg, CMBIS estimates

SELL (Maintain)

Target Price	HK\$29.0
(Previous TP	HK\$35.8)
Up/Downside	-31%
Current Price	HK\$42.2

China Technology Sector

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Stock Data

Mkt. Cap. (HK\$m)	50,999
Avg. 3mths t/o (HK\$m)	653.26
52W High/Low (HK\$)	72.90/ 32.85
Total Issued Shares (mn)	1,209
Source: Bloomberg	

Shareholding Structure

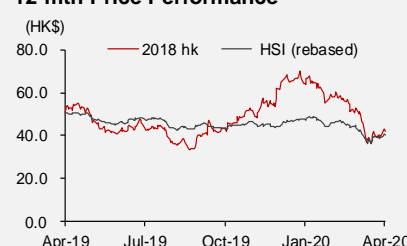
Chunyan Wu	21.75%
Zhengmin Pan	19.24%
JPMorgan Chase	12.39%
Source: HKEx	

Share Performance

	Absolute	Relative
1-mth	-18.1%	-11.7%
3-mth	-33.0%	-21.7%
6-mth	-0.9%	5.5%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Deloitte Touche Tohmatsu

Related Reports:

1. AAC Tech (2018 HK) – Awaiting better visibility in 2Q – 26 Mar 2020
2. AAC Tech (2018 HK) – Worst is likely over but most positives are priced in – 11 Nov 2019
3. AAC Tech (2018 HK) – Outlook remains challenging; Maintain Sell - 26 Aug 2019

Earnings Revision

Our FY20/21E EPS are 32%/22% below consensus

We cut our FY20-22E EPS by 4-19% to reflect lower revenue and margin assumptions. Our EPS are lower than consensus by 22-32% mainly due to more conservative gross margin and revenue estimates for acoustics/haptics/casing segments.

Figure 1: CMBI earnings revisions

RMB mn	New			Old			Change (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	16,456	19,424	20,928	18,060	20,321	21,729	-9%	-4%	-4%
Gross Profit	4,449	5,607	6,165	5,035	5,901	6,401	-12%	-5%	-4%
Operating Profit	1,949	2,843	3,187	2,419	3,010	3,309	-19%	-6%	-4%
Net profit	1,751	2,561	2,881	2,161	2,718	2,997	-19%	-6%	-4%
EPS (RMB)	1.45	2.12	2.38	1.79	2.25	2.48	-19%	-6%	-4%
Gross Margin	27.0%	28.8%	29.4%	27.9%	29.0%	29.4%	-0.8 ppt	-0.2 ppt	0 ppt
Operating Margin	11.8%	14.6%	15.2%	13.4%	14.8%	15.2%	-1.5 ppt	-0.2 ppt	0 ppt
Net Margin	10.6%	13.2%	13.8%	12.0%	13.4%	13.8%	-1.3 ppt	-0.2 ppt	0 ppt

Source: Company data, CMBIS estimates

Figure 2: CMBI estimates vs consensus

RMB mn	CMBI			Consensus			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	16,456	19,424	20,928	19,724	23,325	23,325	-17%	-17%	-10%
Gross Profit	4,449	5,607	6,165	5,749	7,113	7,113	-23%	-21%	-13%
Operating Profit	1,949	2,843	3,187	2,918	3,667	3,667	-33%	-22%	-13%
Net profit	1,751	2,561	2,881	2,580	3,261	3,261	-32%	-21%	-12%
EPS (RMB)	1.45	2.12	2.38	2.14	2.70	2.70	-32%	-22%	-12%
Gross Margin	27.0%	28.8%	29.4%	29.1%	30.5%	30.5%	-2.1 ppt	-1.7 ppt	-1.1 ppt
Operating Margin	11.8%	14.6%	15.2%	14.8%	15.7%	15.7%	-2.9 ppt	-1.1 ppt	-0.5 ppt
Net Margin	10.6%	13.2%	13.8%	13.1%	14.0%	14.0%	-2.4 ppt	-0.8 ppt	-0.2 ppt

Source: Bloomberg, CMBIS estimates

Figure 3: Revenue breakdown

RMB mn	FY18	FY19	1Q20E	2Q20E	3Q20E	4Q20E	FY20E	FY21E	FY22E
Revenue									
Dynamic components	8,675	8,167	1,042	1,564	2,161	2,045	6,811	7,444	7,813
MEMS components	814	929	131	249	318	285	983	1,032	1,084
Haptics & RF	8,073	7,694	815	1,419	1,858	2,706	6,798	7,590	7,685
Others (incl. optics)	569	1,094	230	421	531	682	1,864	3,358	4,347
Total	18,131	17,884	2,217	3,652	4,869	5,717	16,456	19,424	20,928
Revenue mix									
Dynamic components	48%	46%	47%	43%	44%	36%	41%	38%	37%
MEMS components	4%	5%	6%	7%	7%	5%	6%	5%	5%
Haptics & RF	45%	43%	37%	39%	38%	47%	41%	39%	37%
Others (incl. optics)	3%	6%	10%	12%	11%	12%	11%	17%	21%
YoY Growth (%)									
Dynamic components	-9%	-6%	-45%	-11%	-5%	-9%	-17%	9%	5%
MEMS components	-4%	14%	-15%	10%	10%	10%	6%	5%	5%
Haptics & RF	-22%	-5%	-47%	-5%	-12%	10%	-12%	12%	1%
Others (incl. optics)	63%	92%	22%	29%	64%	97%	70%	80%	29%
Total	-14%	-1%	-41%	-4%	-3%	8%	-8%	18%	8%
Gross profit margin									
Dynamic components	37.2%	31.0%	26.0%	26.0%	32.0%	29.5%	29.0%	30.0%	31.0%
MEMS components	26.6%	27.5%	19.0%	26.0%	30.5%	30.0%	27.7%	28.5%	29.0%
Haptics & RF	40.6%	29.6%	30.1%	25.4%	29.1%	29.3%	28.5%	30.3%	30.4%
Others (incl. optics)	4.0%	3.2%	8.0%	10.0%	15.0%	18.0%	14.1%	23.0%	25.0%
Total	37.2%	28.6%	25.2%	23.9%	28.9%	28.0%	27.0%	28.8%	29.4%

Source: Company data, CMBIS

Figure 4: P&L forecast

RMB mn	FY18	FY19	1Q20E	2Q20E	3Q20E	4Q20E	FY20E	FY21E	FY22E
Revenue	18,131	17,884	2,217	3,652	4,869	5,717	16,456	19,424	20,928
...YoY	-14.1%	-1.4%	-40.9%	-4.3%	-2.8%	7.8%	-8.0%	18.0%	7.7%
Cost of sales	(11,388)	(12,777)	(1,658)	(2,779)	(3,460)	(4,114)	(12,011)	(13,823)	(14,770)
Gross profit	6,743	5,107	559	874	1,409	1,603	4,445	5,601	6,159
GPM (%)	37.2%	28.6%	25.2%	23.9%	28.9%	28.0%	27.0%	28.8%	29.4%
...YoY	-22.7%	-24.3%	-50.5%	-8.5%	-5.0%	4.1%	-13.0%	26.0%	10.0%
SG&A	(966)	(918)	(182)	(176)	(214)	(307)	(879)	(1,010)	(1,088)
...% of rev	-5.3%	-5.1%	-8.2%	-4.8%	-4.4%	-5.4%	-5.3%	-5.2%	-5.2%
R&D	(1,512)	(1,717)	(310)	(402)	(419)	(486)	(1,617)	(1,748)	(1,884)
...% of rev	-8.3%	-9.6%	-14.0%	-11.0%	-8.6%	-8.5%	-9.8%	-9.0%	-9.0%
Operating	4,265	2,472	67	296	776	810	1,949	2,843	3,187
OPM (%)	23.5%	13.8%	3.0%	8.1%	15.9%	14.2%	11.8%	14.6%	15.2%
...YoY	-29.9%	-42.0%	-86.3%	-16.4%	-6.3%	1.1%	-21.2%	45.9%	12.1%
Net profit	3,796	2,222	62	277	648	765	1,751	2,561	2,881
NPM (%)	20.9%	12.4%	2.8%	7.6%	13.3%	13.4%	10.6%	13.2%	13.8%
...YoY	-28.7%	-41.5%	-85.8%	-17.9%	-6.9%	1.0%	-21.2%	46.2%	12.5%

Source: Company data, CMBIS

Valuation

Maintain Sell with new TP HK\$29.0 (31% downside)

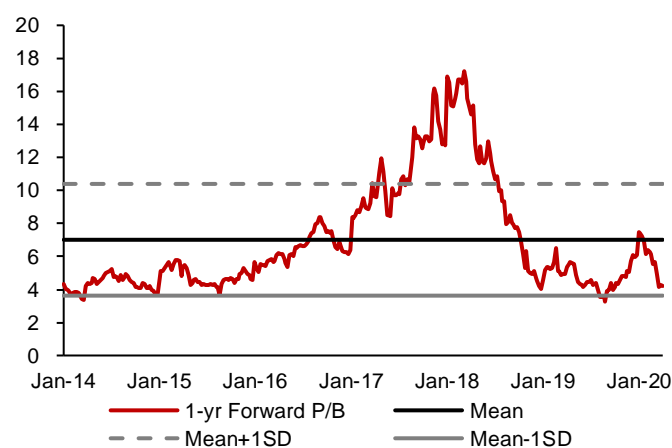
We maintain Sell for our cautious view on iPhone launch delay, optics guidance and order uncertainty. Although recent 40% correction have reflected 1H20 weakness and COVID-19 supply impact, we believe there is still downside on consensus earnings due to product launch delays and demand weakness. Our new TP of HK\$29.0 is based on same 18x FY20E P/E. Upside risks include stronger lens, better iPhone and better GPM.

Figure 5: 12M forward P/E band



Source: Company data, CMBIS

Figure 6: 12M forward P/B band



Source: Company data, CMBIS

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	18,131	17,884	16,456	19,424	20,928
COGS	(11,388)	(12,777)	(12,011)	(13,823)	(14,770)
Gross profit	6,743	5,107	4,445	5,601	6,159
Selling and marketing	(317)	(275)	(263)	(330)	(356)
Administrative	(650)	(643)	(615)	(680)	(732)
R&D	(1,512)	(1,717)	(1,617)	(1,748)	(1,884)
Operating profit	4,265	2,472	1,949	2,843	3,187
Financial cost	(218)	(248)	(248)	(248)	(248)
Other income/(losses)	264	329	310	315	335
Pre-tax profit	4,310	2,552	2,010	2,910	3,274
Tax	(514)	(330)	(259)	(349)	(393)
Minority interest	-	-	-	-	-
Net profit	3,796	2,222	1,751	2,561	2,881

Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Profit before taxation	4,310	2,552	2,010	2,910	3,274
Depreciation	1,750	1,803	2,003	2,203	2,403
Change in working capital	1,149	(627)	957	(2,396)	1,844
Others	(420)	(85)	(27)	(67)	(128)
Net cash from operating	6,789	3,644	4,944	2,650	7,394
Capex	(2,941)	(3,000)	(2,800)	(2,800)	(2,800)
Other	(658)	68			
Net cash from investing	(3,599)	(2,932)	(2,800)	(2,800)	(2,800)
Net borrowings	(555)	0	0	0	0
Interest paid	(216)	(248)	(248)	(248)	(248)
Dividend paid	(2,182)	(1,531)	(1,206)	(896)	(1,008)
Other	(294)	0	0	0	0
Net cash from financing	(3,247)	(1,779)	(1,455)	(1,145)	(1,256)
Net change in cash	(57)	(1,068)	690	(1,295)	3,337
Cash at beg of year	4,034	4,059	2,991	3,681	2,386
Exchange difference	81	0	0	0	0
Cash at end of year	4,059	2,991	3,681	2,386	5,723

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Current assets	11,985	11,918	10,400	13,631	13,895
Cash & equivalents	4,126	2,991	3,681	2,386	5,723
Trade and other rev.	4,474	6,930	3,650	8,505	4,713
Inventories	3,319	1,931	3,005	2,676	3,394
Other current assets	65	65	65	65	65
Non-current assets	17,884	19,080	19,877	20,474	20,870
PPE	15,440	16,637	17,433	18,030	18,426
Lease prepayments	622	622	622	622	622
Intangible assets	367	367	367	367	367
Other non-curr. assets	1,455	1,455	1,455	1,455	1,455
Total assets	29,869	30,998	30,277	34,105	34,765
Current liabilities	8,317	8,754	7,489	9,652	8,439
Short-term borrowings	3,493	3,493	3,493	3,493	3,493
Trade & other payables	4,548	4,989	3,739	5,868	4,639
Tax payables	205	202	186	219	236
Other current liabilities	71	71	71	71	71
Non-current liabilities	2,618	2,618	2,618	2,618	2,618
Government grants	118	118	118	118	118
Deferred tax liabilities	72	72	72	72	72
Other non-current liab.	2,429	2,429	2,429	2,429	2,429
Total liabilities	10,935	11,373	10,107	12,270	11,057
Share capital	99	99	99	99	99
Reserves	18,835	19,527	20,072	21,736	23,609
Minority interest					
Shareholders' equity	18,934	19,626	20,170	21,835	23,708
Total equity & liabilities	29,869	30,998	30,277	34,105	34,765

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Dynamic components	47.8	45.7	41.4	38.3	37.3
MEMS (microphone)	4.5	5.2	6.0	5.3	5.2
Electro. (haptics)	44.5	43.0	41.3	39.1	36.7
Other	3.1	6.1	11.3	17.3	20.8
Growth (%)					
Revenue	(14.1)	(1.4)	(8.0)	18.0	7.7
Gross profit	(22.7)	(24.3)	(13.0)	26.0	10.0
Operating Income	(29.9)	(42.0)	(21.2)	45.9	12.1
Net profit	(28.7)	(41.5)	(21.2)	46.2	12.5
Profitability (%)					
Gross Margin	37.2	28.6	27.0	28.8	29.4
Operating Margin	23.5	13.8	11.8	14.6	15.2
Net margin	20.9	12.4	10.6	13.2	13.8
Balance sheet ratios					
Net debt/total equity (x)	0.1	0.1	0.1	0.2	0.0
Current ratio (x)	1.4	1.4	1.4	1.4	1.6
Receivable turnover days	88	90.0	90.0	90.0	90.0
Inventory turnover days	89	75.0	75.0	75.0	75.0
Payable turnover days	85	70.0	70.0	70.0	70.0
Returns (%)					
ROE	20.0	11.3	8.7	11.7	12.2
ROA	12.7	7.2	5.8	7.5	8.3
Per share data (RMB)					
EPS	3.12	1.84	1.45	2.12	2.38
DPS	1.79	1.27	1.00	0.74	0.83

Source: Company data, CMBIS estimates

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