

# Jiangsu Hengli (601100 CH)

## 2Q19 earnings slowed but in line with estimate

Hengli's net profit in 1H19 grew 45% YoY to RMB671mn. In 2Q19, net profit grew 12% YoY to RMB345mn, which is largely in line with expectation as the weak demand in 2Q had been expected. Gross margin expansion is a surprise, suggesting that the pricing power of Hengli remains strong. Besides, operating cash flow grew 3.1x YoY to RMB795mn in 1H19, higher than the net profit. We understand that the order intakes in Aug improved compared with that in Jul. We continue to like Hengli for its import substitution story on hydraulic cylinder, pump and valve. The stock is now trading at 21x 2019E P/E, the mid-point of valuation over the past two years.

- Revenue grew 29% YoY to RMB2.79bn in 1H19**, driven by (1) 25% YoY revenue growth of hydraulic cylinder for excavator, (2) 8% YoY increase in non-standardized hydraulic cylinder for heavy equipment; (3) 57% YoY increase in other product revenue (helped by 100% YoY increase in hydraulic pump and valve. While revenue in 2Q19 grew only ~3% YoY, the weakness has been largely expected.
- Sales volume and ASP.** Hengli's sales volume of hydraulic cylinder for excavator grew 13% YoY to 256k units in 1H19. The growth was largely in line with China's excavator sales volume growth of 14%, according to CCMA data. Hengli's non-standardized hydraulic cylinder increased 18% YoY to 78.6k units. Most importantly, the ASP of hydraulic cylinder for excavator increased 11% YoY to RMB4.8k / unit.
- Gross margin expansion a result of strong pricing power and product mix improvement.** Gross margin expanded 2.4ppt YoY to 37% in 1H19. In 2Q19, the gross margin reached 39.9%, up from 34.8% in 1Q19. Margin expansion was the key reason for the earnings growth in 2Q19.
- Operating cash flow grew significantly.** The 3.1x YoY in operating cash flow was due to the Company's strong execution in cash collection.
- Key risks.** (1) weakness in demand for excavators; (2) increase in component cost.

### Earnings Summary

(YE 31 Dec)	FY16A	FY17A	FY18A
Revenue (RMB mn)	1,370	2,795	4,211
YoY growth (%)	26.0	104.0	50.6
Net income (RMB mn)	70	382	837
EPS (RMB)	0.08	0.43	0.95
YoY growth (%)	10.8	442.9	119.1
EV/EBITDA (x)	156.7	38.5	22.9
P/E (x)	358.6	66.0	30.2
P/B (x)	7.2	6.6	5.5
Yield (%)	0.2	0.5	1.2
ROE (%)	2.0	10.4	19.9
Net gearing (%)	3.3	5.0	Net cash

Source: Company data, CMBIS estimates

**NOT RATED**

Current Price

RMB28.6

### China Capital Goods

#### Wayne Fung, CFA

(852) 3900 0826

waynefung@cmbi.com.hk

#### Stock Data

Mkt Cap (RMB mn)	25,225
Avg 3 mths t/o (RMB mn)	129
52w High/Low (RMB)	34.55/17.20
Total Issued Shares (mn)	882

Source: Bloomberg

#### Shareholding Structure

WANG's family	71.0%
CCASS (Hong Kong)	6.5%
Deutsche Bank AG	2.2%
Free float	20.3%

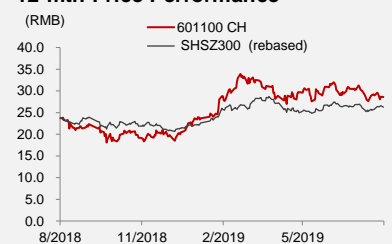
Source: Company data

#### Share Performance

	Absolute	Relative
1-mth	-5.0%	-4.3%
3-mth	-3.4%	-9.1%
6-mth	-0.4%	-2.8%

Source: Bloomberg

#### 12-mth Price Performance



Source: Bloomberg

Auditor: RSM

**Figure 1: Key highlights of 1H19 results**

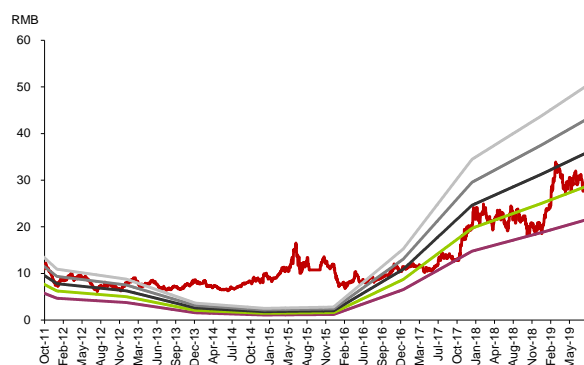
YE Dec 31(RMB mn)	1H18	1H19	Change (YoY)
<b>Total revenue</b>	<b>2,164</b>	<b>2,793</b>	<b>29.0%</b>
Cost of sales	(1,415)	(1,759)	24.3%
<b>Gross profit</b>	<b>749</b>	<b>1,034</b>	<b>38.1%</b>
Surcharge	(23)	(25)	8.3%
S&D expenses	(48)	(48)	-0.2%
Administrative expenses	(160)	(208)	30.3%
Asset impairment	(11)	(13)	20.0%
<b>EBIT</b>	<b>506</b>	<b>739</b>	<b>46.0%</b>
Net finance income/(cost)	(4)	14	n/a
Finance income	26	103	297.5%
Finance expenses	(30)	(88)	193.8%
Other gains/(losses)	37	25	-32.0%
Share of profit of JV and associates	0	0	n/a
<b>Pretax profit</b>	<b>539</b>	<b>778</b>	<b>44.5%</b>
Income tax	(74)	(107)	43.6%
<b>After tax profit</b>	<b>465</b>	<b>672</b>	<b>44.6%</b>
MI	(1)	(1)	2.6%
<b>Net profit</b>	<b>463</b>	<b>671</b>	<b>44.7%</b>
D&A	110	124	12.6%
<b>EBITDA</b>	<b>617</b>	<b>864</b>	<b>40.0%</b>

Source: Company data, CMBIS

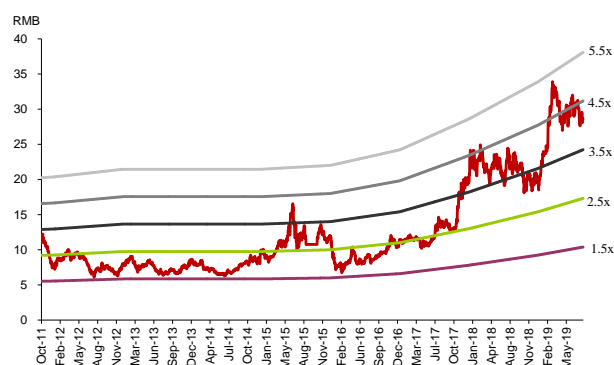
**Figure 2: Key highlights of 2Q19 results**

(RMB mn)	1Q18	1Q19	Change YoY	2Q18	2Q19	Change YoY
<b>Total revenue</b>	<b>970</b>	<b>1,569</b>	<b>61.6%</b>	<b>1,194</b>	<b>1,224</b>	<b>2.6%</b>
Cost of sales	(641)	(1,023)	59.7%	(775)	(736)	-5.0%
<b>Gross profit</b>	<b>330</b>	<b>546</b>	<b>65.5%</b>	<b>419</b>	<b>488</b>	<b>16.6%</b>
Other income	(10)	(15)	46.7%	(13)	(11)	-20.2%
S&D expenses	(23)	(19)	-17.0%	(25)	(29)	15.5%
Administrative expenses	(74)	(95)	28.3%	(86)	(113)	32.1%
Asset impairment	(8)	(21)	171.1%	(3)	8	n/a
<b>EBIT</b>	<b>214</b>	<b>395</b>	<b>84.3%</b>	<b>292</b>	<b>344</b>	<b>17.8%</b>
Net finance income/(cost)	(49)	(35)	-27.7%	45	50	11.3%
Other gains/(loss)	15	13	-13.6%	21	12	-45.2%
Share of profit of JV and associates	0	0	n/a	0	0	n/a
<b>Pretax profit</b>	<b>181</b>	<b>373</b>	<b>106.3%</b>	<b>358</b>	<b>405</b>	<b>13.3%</b>
Income tax	(24)	(47)	94.2%	(50)	(60)	19.5%
<b>After tax profit</b>	<b>157</b>	<b>327</b>	<b>108.2%</b>	<b>308</b>	<b>345</b>	<b>12.2%</b>
MI	(0)	(0)	384.4%	(1)	(1)	-33.2%
<b>Net profit</b>	<b>157</b>	<b>326</b>	<b>108.0%</b>	<b>307</b>	<b>345</b>	<b>12.4%</b>

Source: Company data, CMBIS

**Figure 3: 12M forward P/E band**

Source: Company data, CMBIS

**Figure 4: 12M forward P/B band**

Source: Company data, CMBIS

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Address: 45/F, Champion Tower, 3 Garden Road, Hong Kong, Tel: (852) 3900 0888 Fax: (852) 3900 0800

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