

AAC Technologies (2018 HK)

3Q20 another miss; Optics likely to improve but hard to move the needle

AAC's 3Q20 net profit declined 32% YoY to RMB425mn, 25%/32% below our/consensus estimates, mainly due to 1) weaker revenue (-10% YoY) on iPhone launch delay, Huawei ban and de-spec trend, 2) lower GPM at 23.6% (vs our est./cons. of 27%/27.4%) across major segments, 3) slower optics ramp (40-50kk/m, vs 80-90kk/m guided) and weaker margin (24.6%, vs 35% guided). While mgmt. toned down optics GPM target to 30%/40% in 4Q20/2021E, we expect further downside on optics' ASP/margin given slower 6P ramp, WLG launch delay and intense competition in mid/low-end optics. We trimmed our FY20-22E EPS by 11-21% and our FY20-22E EPS are 17-28% below consensus. Maintain Hold with new SOTP-based TP HK\$43.2 given fair valuation at 24.7x FY21E P/E and slower-than-expected optics progress.

- **3Q20 another miss; GPM surprises on the downside.** AAC's 3Q20 net profit dropped 32% YoY, 25%/32% below our/consensus estimates, while revenue fell 10% YoY to RMB4.5bn due to iPhone launch delays and slower spec upgrade on acoustics/haptics/casings. GPM came in at 23.6%, well below our/consensus of 27%, given GPM pressure across acoustic/haptic/casing segments.
- **Optics: weaker volume/margin growth; Lower ASP amid de-spec trend.** Although 3Q20 optics shipment reached 40-50kk/m (vs 30-40kk/m in 2Q20) and GPM improved to 24.6% (vs 13.8% in 2Q20), the progress was still behind mgmt's guidance of 80-90kk/m and 35% GPM. Given ongoing de-spec trend, Huawei impact (AAC's No. 2 lens client) and intense competition in mid/low-end lens with Sunny/Largan/O-Film, we expect ASP/margin will remain under pressure in near term.
- **2021: better iPhone volume but lack of upgrade across all segments.** While we think AAC will benefit from iPhone 12 cycle with stabilizing share allocation, we believe its acoustic/haptics (34% of FY20E sales) will continue to face ASP pressure for lack of upgrade, and its casing segment (Huawei mainly, 15% of sales) will decline given 2H20 Huawei impact. We estimate 4Q20E net profit to decline 25% YoY on revenue growth of 2% YoY.
- **Our FY20/21E EPS are 26%/28% below consensus; Maintain HOLD.** We trimmed FY20-22E EPS by 11-21% for weaker optics/casing due to Huawei impact and lower GPM on slower upgrade. Our SOTP-based TP is lowered to HK\$43.2, implying 23.7x FY21E P/E. Upside risks include better optics margin and stronger iPhone shipment.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	18,131	17,884	17,767	19,829	20,348
YoY growth (%)	(14.1)	(1.4)	(0.7)	11.6	2.6
Net income (RMB mn)	3,796	2,222	1,317	1,973	2,276
EPS (RMB)	3.12	1.84	1.09	1.63	1.88
YoY growth (%)	(28.5)	(41.1)	(40.7)	49.9	15.4
Consensus EPS (RMB)	NA	1.84	1.48	2.27	2.74
P/E (x)	12.9	21.9	37.0	24.7	21.4
P/B (x)	2.6	2.5	2.4	2.3	2.2
Yield (%)	4.4	3.1	1.4	2.0	2.3
ROE (%)	20.0	11.3	6.5	9.3	10.2

Source: Company data, Bloomberg, CMBIS estimates

HOLD (Maintain)

Target Price	HK\$43.2
(Previous TP	HK\$47.5)
Up/Downside	-4%
Current Price	HK\$44.9

China Technology Sector

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Stock Data

Mkt. Cap. (HK\$m)	54,262
Avg. 3mths t/o (HK\$m)	443.38
52W High/Low (HK\$)	72.90/ 35.6
Total Issued Shares (mn)	1,209

Source: Bloomberg

Shareholding Structure

Chunyuan Wu	21.75%
Zhengmin Pan	19.24%
JPMorgan Chase	11.51%

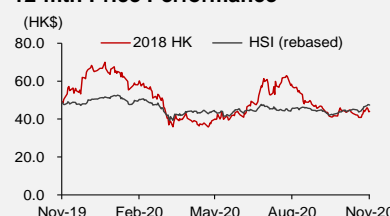
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-0.9%	-6.7%
3-mth	-22.9%	-25.6%
6-mth	10.0%	1.9%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Deloitte Touche Tohmatsu

Related Reports:

1. AAC Tech (2018 HK) - Further strategic investments into AAC Optics; Expect ASP/margin pressure to persist – 12 Oct 2020
2. AAC Tech (2018 HK) – 2Q20 another miss; Maintain Hold on slower optics in near term - 25 Aug 2020
3. AAC Tech (2018 HK) – Strategic investors to boost synergy and unlock value; Upgrade to HOLD – 23 Jul 2020

3Q20 Results Review

Figure 1: 3Q20 results review

RMB mn	3Q19	2Q20	3Q20	QoQ	YoY	CMBIS 3Q20E	Diff %	Consensus 3Q20E	Diff %
Revenue	5,012	4,277	4,520	6%	-10%	5,242	-14%	4,946	-9%
Gross Profit	1,483	995	1,067	21%	-28%	1,435	-26%	1,336	-20%
Operating Profit	829	262	376	176%	-55%	687	-45%	683	-45%
Net profit	695	268	425	409%	-39%	626	-32%	569	-25%
EPS (RMB)	0.57	0.22	0.35	409%	-39%	0.51	-31%	0.47	-25%
Margin (%)									
Gross Margin	29.6%	23.3%	23.6%		-6.0 ppt	27.4%	-3.8 ppt	27.0%	-3.4 ppt
Operating Margin	16.5%	6.1%	8.3%		-8.2 ppt	13.1%	-4.8 ppt	13.8%	-5.5 ppt
Net Margin	13.9%	6.3%	9.4%		-4.5 ppt	11.9%	-2.5 ppt	11.5%	-2.1 ppt
Growth (%)									
Revenue (YoY)	3%	12%	-10%			5%		-1%	
Revenue (QoQ)	31%	-76%	27%			23%		39%	
Operating profit	-29%	-26%	-55%			-17%		-18%	
Net profit	-29%	-21%	-39%			-10%		-18%	

Source: Company data, Bloomberg, CMBIS

Figure 2: Revenue breakdown

RMB mn	FY18	FY19	1Q20	2Q20	3Q20	4Q20E	FY20E	FY21E	FY22E
Revenue									
Dynamic components	8,675	8,167	1,421	1,908	2,159	2,172	7,660	7,868	7,930
MEMS components	814	929	199	259	368	285	1,111	1,166	1,224
Haptics & RF	8,073	7,694	1,691	1,725	1,515	2,254	7,184	7,734	7,688
Others (incl. optics)	569	1,094	249	385	478	700	1,813	3,061	3,506
Total	18,131	17,884	3,560	4,277	4,520	5,410	17,767	19,829	20,348
Revenue mix									
Dynamic components	48%	46%	40%	45%	48%	40%	43%	40%	39%
MEMS components	4%	5%	6%	6%	8%	5%	6%	6%	6%
Haptics & RF	45%	43%	47%	40%	34%	42%	40%	39%	38%
Others (incl. optics)	3%	6%	7%	9%	11%	13%	10%	15%	17%
YoY Growth (%)									
Dynamic components	-9%	-6%	-24%	8%	-5%	-3%	-6%	3%	1%
MEMS components	-4%	14%	29%	14%	27%	10%	20%	5%	5%
Haptics & RF	-22%	-5%	11%	11%	-28%	-8%	-7%	8%	-1%
Others (incl. optics)	63%	92%	32%	41%	47%	102%	66%	69%	15%
Total	-14%	-1%	-5%	12%	-10%	2%	-1%	12%	3%
Gross profit margin									
Dynamic components	37.2%	31.0%	26.0%	26.4%	26.6%	27.0%	26.6%	27.0%	27.0%
MEMS components	26.6%	27.5%	16.5%	16.1%	19.0%	20.0%	18.1%	24.0%	26.0%
Haptics & RF	40.6%	29.6%	23.6%	22.8%	20.1%	22.4%	22.3%	22.8%	23.7%
Others (incl. optics)	4.0%	3.2%	9.5%	13.8%	24.7%	28.1%	21.6%	31.0%	35.0%
Total	37.2%	28.6%	23.1%	23.3%	23.6%	24.8%	23.8%	25.8%	27.1%

Source: Company data, CMBIS

Earnings Revision

Figure 3: CMBIS earnings revisions

RMB mn	New			Old			Change (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	17,767	19,829	20,348	18,329	21,051	21,670	-3%	-6%	-6%
Gross Profit	4,233	5,124	5,518	4,761	5,710	6,076	-11%	-10%	-9%
Operating Profit	1,326	2,184	2,521	1,873	2,589	2,885	-29%	-16%	-13%
Net profit	1,317	1,973	2,276	1,675	2,296	2,564	-21%	-14%	-11%
EPS (RMB)	1.09	1.63	1.88	1.39	1.90	2.12	-21%	-14%	-11%
Gross Margin	23.8%	25.8%	27.1%	25.9%	27.1%	28.0%	-2.1 ppt	-1.3 ppt	-0.9 ppt
Operating Margin	7.5%	11.0%	12.4%	10.2%	12.3%	13.3%	-2.8 ppt	-1.3 ppt	-0.9 ppt
Net Margin	7.4%	9.9%	11.2%	9.1%	10.9%	11.8%	-1.7 ppt	-1 ppt	-0.6 ppt

Source: Company data, CMBIS estimates

Figure 4: CMBIS estimates vs consensus

RMB mn	CMBIS			Consensus			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	17,767	19,829	20,348	18,876	22,209	22,209	-6%	-11%	-8%
Gross Profit	4,233	5,124	5,518	5,000	6,402	6,402	-15%	-20%	-14%
Operating Profit	1,326	2,184	2,521	2,026	3,212	3,212	-35%	-32%	-22%
Net profit	1,317	1,973	2,276	1,836	2,791	2,791	-28%	-29%	-18%
EPS (RMB)	1.09	1.63	1.88	1.48	2.27	2.27	-26%	-28%	-17%
Gross Margin	23.8%	25.8%	27.1%	26.5%	28.8%	28.8%	-2.7 ppt	-3 ppt	-1.7 ppt
Operating Margin	7.5%	11.0%	12.4%	10.7%	14.5%	14.5%	-3.3 ppt	-3.5 ppt	-2.1 ppt
Net Margin	7.4%	9.9%	11.2%	9.7%	12.6%	12.6%	-2.3 ppt	-2.6 ppt	-1.4 ppt

Source: Bloomberg, CMBIS estimates

Figure 5: P&L forecast

RMB mn	FY18	FY19	1Q20	2Q20	3Q20	4Q20E	FY20E	FY21E	FY22E
Revenue	18,131	17,884	3,560	4,277	4,520	5,410	17,767	19,829	20,348
...YoY	-14.1%	-1.4%	-5.1%	12.1%	-9.8%	2.0%	-0.7%	11.6%	2.6%
Cost of sales	(11,388)	(12,777)	(2,737)	(3,282)	(3,453)	(4,066)	(13,538)	(14,711)	(14,836)
Gross profit	6,743	5,107	823	995	1,067	1,344	4,229	5,118	5,512
GPM (%)	37.2%	28.6%	23.1%	23.3%	23.6%	24.8%	23.8%	25.8%	27.1%
...YoY	-22.7%	-24.3%	-27.1%	4.2%	-28.1%	-12.7%	-17.2%	21.0%	7.7%
SG&A	(966)	(918)	(239)	(240)	(239)	(291)	(1,007)	(1,031)	(1,058)
...% of rev	-5.3%	-5.1%	-6.7%	-5.6%	-5.3%	-5.4%	-5.7%	-5.2%	-5.2%
R&D	(1,512)	(1,717)	(489)	(494)	(452)	(460)	(1,895)	(1,904)	(1,933)
...% of rev	-8.3%	-9.6%	-13.7%	-11.5%	-10.0%	-8.5%	-10.7%	-9.6%	-9.5%
Operating profit	4,265	2,472	95	262	376	594	1,326	2,184	2,521
OPM (%)	23.5%	13.8%	2.7%	6.1%	8.3%	11.0%	7.5%	11.0%	12.4%
...YoY	-29.9%	-42.0%	-80.5%	-25.9%	-54.6%	-25.9%	-46.3%	64.6%	15.5%
Net profit	3,796	2,222	53	268	425	571	1,317	1,973	2,276
NPM (%)	20.9%	12.4%	1.5%	6.3%	9.4%	10.5%	7.4%	9.9%	11.2%
...YoY	-28.7%	-41.5%	-87.8%	-20.8%	-38.8%	-24.6%	-40.8%	49.9%	15.4%

Source: Company data, CMBIS

Valuation

Maintain HOLD with new TP HK\$43.2

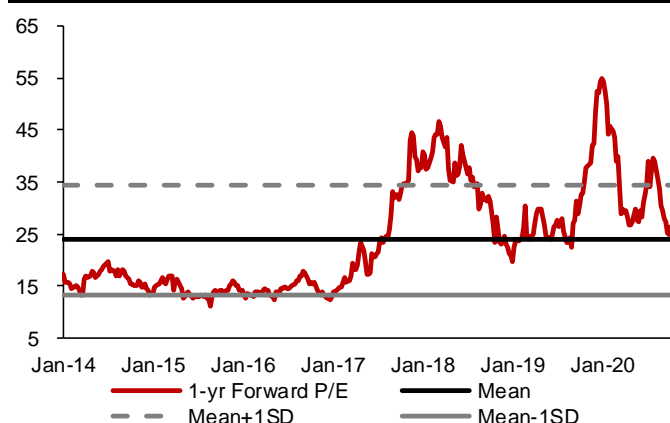
We derived our new TP of HK\$ 43.2 based on SOTP to reflect business diversification with different growth profiles and visibility. Our new TP is based on weighted-average target P/E multiple of 23.2x FY21E EPS and valuation of optics segment at RMB 17.9bn. We assign 20x P/E to AAC's core businesses, including acoustics, MEMS, haptics and mechanical RF, in-line with HK-listed peers.

Figure 6: AAC Tech – SOTP valuation

Business segment	Value per share (RMB)	Valuation Methodology	Target P/E	% of FY21E Profit	FY21E EPS (RMB)
Acoustics	13.6	P/E target multiple	20x	42%	0.68
MEMS	1.8	P/E target multiple	20x	5%	0.09
ED & PM	11.3	P/E target multiple	20x	34%	0.56
Optics	12.1	82% of RMB 17.9bn			0.30
TP (RMB)	42.6		22.4x		1.63
TP (HK\$)	47.5				

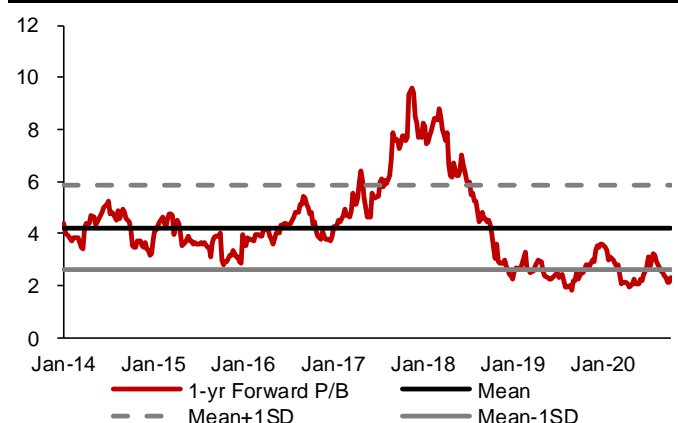
Sources: Company data, CMBIS

Figure 7: 12M forward P/E band



Source: Company data, CMBIS

Figure 8: 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	17,767	19,829	20,348
COGS	(11,388)	(12,777)	(13,538)	(14,711)	(14,836)
Gross profit	6,743	5,107	4,229	5,118	5,512
Selling and marketing	(317)	(275)	(301)	(317)	(326)
Administrative	(650)	(643)	(706)	(714)	(733)
R&D	(1,512)	(1,717)	(1,895)	(1,904)	(1,933)
Operating profit	4,265	2,472	1,326	2,184	2,521
Financial cost	(218)	(248)	(319)	(319)	(319)
Other income/(losses)	264	329	562	378	385
Pre-tax profit	4,310	2,552	1,569	2,242	2,587
Tax	(514)	(330)	(252)	(269)	(310)
Minority interest	-	-	0	0	0
Net profit	3,796	2,222	1,317	1,973	2,276

Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Profit before taxation	4,310	2,552	1,569	2,242	2,587
Depreciation	1,750	1,803	2,003	2,203	2,403
Change in working capital	1,149	(627)	332	(1,287)	1,152
Others	(420)	(85)	66	74	15
Net cash from operating	6,789	3,644	3,970	3,232	6,158
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)	-	-	-	-
Interest paid	(216)	(248)	(319)	(319)	(319)
Dividend paid	(2,182)	(1,531)	(658)	(986)	(1,138)
Other	(294)	-	-	-	-
Net cash from financing	(3,247)	(1,779)	(978)	(1,306)	(1,457)
Net change in cash	(57)	(1,068)	192	(874)	1,900
Cash at beg of year	4,034	4,059	2,991	3,184	2,310
Exchange difference	81	-	-	-	-
Cash at end of year	4,059	2,991	3,184	2,310	4,210

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Current assets	11,985	11,918	11,272	12,875	12,791
Cash & equivalents	4,126	2,991	3,184	2,310	4,210
Trade and other rev.	4,474	6,930	4,391	8,087	4,832
Inventories	3,319	1,931	3,632	2,413	3,684
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	31,149	33,349	33,661
Current liabilities	8,317	8,754	8,247	9,460	8,633
Short-term borrowings	3,493	3,493	3,493	3,493	3,493
Trade & other payables	4,548	4,989	4,482	5,672	4,840
Tax payables	205	202	201	224	230
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	10,865	12,078	11,252
Share capital	99	99	99	99	99
Reserves	18,835	19,527	20,185	21,171	22,309
Minority interest	-	-	-	-	-
Shareholders' equity	18,934	19,626	20,284	21,270	22,408
Total equity & liabilities	29,869	30,998	31,149	33,348	33,660

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Dynamic components	47.8	45.7	43.1	39.7	39.0
MEMS (microphone)	4.5	5.2	6.3	5.9	6.0
Electro. (haptics)	44.5	43.0	40.4	39.0	37.8
Other	3.1	6.1	10.2	15.4	17.2
Growth (%)					
Revenue	(14.1)	(1.4)	(0.7)	11.6	2.6
Gross profit	(22.7)	(24.3)	(17.2)	21.0	7.7
Operating Income	(29.9)	(42.0)	(46.3)	64.6	15.5
Net profit	(28.7)	(41.5)	(40.8)	49.9	15.4
Profitability (%)					
Gross Margin	37.2	28.6	23.8	25.8	27.1
Operating Margin	23.5	13.8	7.5	11.0	12.4
Net margin	20.9	12.4	7.4	9.9	11.2
Balance sheet ratios					
Net debt/total equity (x)	0.1	0.1	0.1	0.2	0.1
Current ratio (x)	1.4	1.4	1.4	1.4	1.5
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	6.5	9.3	10.2
ROA	12.7	7.2	4.2	5.9	6.8
Per share data (RMB)					
EPS	3.12	1.84	1.09	1.63	1.88
DPS	1.79	1.27	0.54	0.82	0.94

Source: Company data, CMBIS estimates

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