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ZTE (763 HK)

ZTE finished 2021 with good results; Positive potentials could materialize ahead

ZTE announced FY21 preliminary results, expecting FY21 net profit to grow 53-69% YoY to RMB6.5bn-7.2bn. Adjusted FY21 net profit is estimated to be ~RMB3.25bn, up 214% YoY. FY21 EPS is expected to be RMB1.44-1.50. Looking forward, we think the company will be a major beneficiary of global 5G deployment and expect ZTE to gain market share in the telecom business. Meanwhile, consumer and government/enterprise segments will continue to deliver good growth. The company is also seeking opportunities in auto electrification, vehicle intelligence, industry digitization, etc. Maintain BUY with TP adjusted to HK\$29.65 based on 15x FY22E P/E.

- FY21 NP grew at 61% YoY despite the delay in 5G deployment. FY21 NP grew at 61% YoY despite the delay in 5G deployment. Overall we think ZTE had a good year in 2021, NP grew 61% YoY despite the postponement of 5G deployment. Implied mid-point 4Q21 net profit is expected to reach RMB1.0bn, representing -33% YoY and -42% QoQ. 4Q21 NP decline was mainly due to one-time asset impairment expenses of RMB1.1bn recorded within this quarter. The company prepares key materials in advance against the backdrop of the global chip shortage. Excluding this, FY21 net profit was in line with our estimates (higher by 1%).
- 5G deployment to continue in the following years. By the end of 2021, 1.425mn 5G base stations were built in China (vs. 588k in 2020), covering 98% of urban areas and 80% of towns, and gradually expanding to all rural areas. According to the 14th Five-Year Plan (2021-2025), 26 5G base stations will be available per 10k users. Although domestic telecom's capex is expected to maintain a similar level in 2022 (vs. 2021), we think ZTE will continue to outperform with additional share gain in overall telecom business.
- Maintain BUY with a new TP of HK\$29.65. We revised down FY22-23E EPS by 11-13%, and adjusted our TP to HK\$29.65 based on the same 15.0x FY22E P/E. We believe the company will enjoy share gain in telcos' 5G-related deployment in the following years. Potential upsides include auto electrification, vehicle intelligence, industry digitization, etc. Risks include US-China disputes, component restriction, and 5G deployment delays.

Earnings Summary

(YE 31 Dec)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue (RMB mn)	90,737	101,451	115,120	129,803	146,400
YoY growth (%)	6.1	11.8	13.5	12.8	12.8
Gross profit margin (%)	37.2	31.6	35.3	35.2	35.2
Net profit (RMB mn)	5,148	4,260	6,818	7,806	8,975
EPS (RMB)	1.22	0.92	1.46	1.64	1.85
YoY growth (%)	NA	-25%	59%	12%	13%
Consensus EPS (RMB)	NA	0.65	1.62	1.79	2.06
PE (x)	14.1	18.7	11.8	10.5	9.3
PB (x)	2.1	1.8	1.6	1.4	1.3
Yield (%)	0.8	0.8	1.3	1.4	1.6
ROE (%)	19.9	11.8	14.7	14.6	14.6
Net debt/total equity (%)	50.0	43.8	46.2	43.8	39.9

Source: Company data, Bloomberg, CMBIS estimates



BUY (Maintain)

Target Price	HK\$ 29.65
(Previous TP	HK\$33.06)
Up/Downside	+43%
Current Price	HK\$ 20.75

China Technology Sector

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Stock Data

Mkt. Cap. (HK\$ mn)	162,515
Avg. 3mths t/o (HK\$ mn)	109
52W High/Low (HK\$)	31.75/18.18
Total Issued Shares (mn)	755.5
Source: Bloomberg	

Shareholding Structure

BlackRock	8.36%
Capital Group	5.08%
Schroders	4.93%
Source: Bloomberg	

Share Performance

	Absolute	Relative
1-mth	0.0%	-2.4%
3-mth	-15.7%	-9.3%
6-mth	-18.2%	-13.8%
Source: Bloombe	erg	

12-mth Price Performance



Source: Bloomberg

Auditor: Ernst & Young

Related Report

- ZTE (763 HK) Expect future share gain under similar 5G capex plan – 16 Oct 2021
- ZTE (763HK) Solid 1H results with strong OCF – 31 Aug 2021



FY21 Results Review

Figure 1: FY21 results review									
RMB mn	2018	2019	2020	2021	YoY				
Revenue	85,513	90,737	101,451						
Gross Profit	28,146	33,728	32,071						
Operating Profit	-612	7,552	5,471						
Net profit	(6,984)	5,148	4,260	6,850	61%				
EPS (RMB)	-1.67	1.22	0.92						
Gross Margin	32.9%	37.2%	31.6%						
Operating Margin	-0.7%	8.3%	5.4%						
Net Margin	-8.2%	5.7%	4.2%						

Source: Company data, CMBIS estimates

Figure 2: CMBIS earnings revisions

	New			Old			Change (%)		
RMB mn	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	115,120	129,803	146,400	116,995	129,879	143,959	-2%	0%	2%
Gross Profit	40,663	45,693	51,515	43,057	47,496	52,841	-6%	-4%	-3%
Operating Profit	8,824	10,192	11,713	9,974	11,313	13,045	-12%	-10%	-10%
Net profit	6,818	7,806	8,975	7,878	8,513	9,822	-13%	-8%	-9%
EPS (RMB)	1.46	1.64	1.85	1.70	1.84	2.12	-14%	-11%	-13%
Gross Margin	35.3%	35.2%	35.2%	36.8%	36.6%	36.7%	-1.5 ppt	-1.4 ppt	-1.5 ppt
Operating Margin	7.7%	7.9%	8.0%	8.5%	8.7%	9.1%	-0.9 ppt	-0.9 ppt	-1.1 ppt
Net Margin	5.9%	6.0%	6.1%	6.7%	6.6%	6.8%	-0.8 ppt	-0.5 ppt	-0.7 ppt

Source: Company data, CMBIS estimates

Figure 3: CMBIS estimates vs consensus

		CMBIS		C	Consensus			Diff (%)	
RMB mn	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	115,120	129,803	146,400	117,416	130,426	144,015	-2%	0%	2%
Gross Profit	40,663	45,693	51,515	42,547	47,157	51,813	-4%	-3%	-1%
Operating Profit	8,824	10,192	11,713	8,646	10,104	11,469	2%	1%	2%
Net profit	6,818	7,806	8,975	7,391	8,134	9,183	-8%	-4%	-2%
EPS (RMB)	1.46	1.64	1.85	1.62	1.79	2.06	-10%	-8%	-10%
Gross Margin	35.3%	35.2%	35.2%	36.2%	36.2%	36.0%	-0.9 ppt	-1 ppt	-0.8 ppt
Operating Margin	7.7%	7.9%	8.0%	7.4%	7.7%	8.0%	0.3 ppt	0.1 ppt	0 ppt
Net Margin	5.9%	6.0%	6.1%	6.3%	6.2%	6.4%	-0.4 ppt	-0.2 ppt	-0.2 ppt

Source: Company data, CMBIS estimates

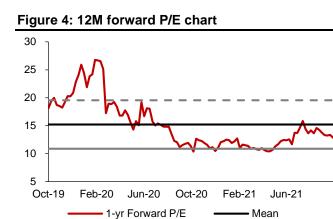
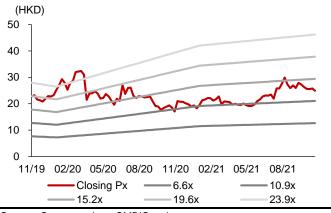


Figure 5: 12M forward P/E band



- - - Mean+1SD Source: Company data, CMBIS estimates

Source: Company data, CMBIS estimates

Mean-1SD



Financial Summary

Income statement						С
YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E	Υ
Revenue	90,737	101,451	115,120	129,803	146,400	Ν
Cost of sales	(57,008)	(69,379)	(74,457)	(84,109)	(94,885)	D
Gross profit	33,728	32,071	40,663	45,693	51,515	С
						С
Selling exp	(7,869)	(7,579)	(8,289)	(9,086)	(10,248)	N
Admin exp	(4,773)	(4,995)	(5,526)	(5,971)	(6,734)	
R&D exp	(12,548)	(14,797)	(18,649)	(21,028)	(23,717)	С
Finance costs	(966)	(421)	(1,094)	(666)	(853)	С
Other operating exp.	1,696	1,573	2,336	2,077	2,656	N
Operating profit	7,552	5,471	8,824	10,192	11,713	
						Ν
Other non-oper exp.	(391)	(407)	(66)	(164)	(185)	D
Pre-tax profit	7,162	5,064	8,758	10,028	11,528	С
						Ν
Income tax expense	(1,385)	(342)	(1,700)	(1,946)	(2,237)	
Minority interests	(280)	(446)	(241)	(275)	(317)	N
Perpetual capital instrument	(349)	(16)	-	-	-	С
Net profit to shareholders	5,148	4,260	6,818	7,806	8,975	E

Cash flow summary					
YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net profit	5,777	4,722	6,818	7,806	8,975
Depreciation/amortization	3,062	3,565	4,592	5,261	5,818
Change in working capital	(4,177)	(1,965)	1,351	(2,030)	996
Others	2,785	3,911	(3,607)	(5,864)	(3,956)
Net cash from operating	7,447	10,233	9,154	5,173	11,832
Capex	6,551	6,472	6,834	7,732	8,281
Other	(12,574)	(13,554)	(6,282)	(10,245)	(9,948)
Net cash from investing	(6,023)	(7,082)	552	(2,513)	(1,667)
Net borrowings	0.040	(4.00.4)	0.007	4 000	(4,005)
õ	9,019	(1,294)	9,267	1,922	(1,025)
Dividend paid	2,640	2,951	2,048	2,672	3,055
Other	(5,938)	(1,947)	(3,194)	(3,394)	(4,161)
Net cash from financing	5,722	(290)	8,120	1,200	(2,131)
Net change in cash	7,372	2,898	17,842	3,416	7,901
Cash at beginning of the year	21,134	28,506	35,660	53,502	56,918
Exchange difference	227	37	16	(444)	(134)
Cash at the end of the year	28,506	31,403	53,502	56,918	64,819

Balance sheet						Key ratios					
YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E	YE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Current assets	102,567	106,977	127,572	141,846	155,992	Revenue mix					
Cash & equivalents	33,309	35,660	53,502	56,918	64,819	Carrier business	66,584	74,018	78,833	87,433	98,189
Account receivables	19,778	15,891	13,627	16,560	18,717	Consumer business	14,997	16,160	17,760	19,552	21,561
Inventory	27,689	33,689	34,028	38,085	39,995	Gov. and enterprise	9,155	11,272	18,526	22,817	26,650
Prepayment	1,023	1,152	1,393	1,507	1,663						
Other current assets	20,768	20,585	25,021	28,776	30,797	Growth (%)					
						Revenue	6.1	11.8	13.5	12.8	12.8
Non-current assets	38,635	43,658	45,419	50,140	53,102	Gross profit	19.8	(4.9)	26.8	12.4	12.7
PPE	9,383	11,914	13,212	14,192	14,992	Operating profit	(1,334.1	(27.6)	61.3	15.5	14.9
Intangible assets	7,719	9,367	7,890	7,829	7,839	Net profit	(173.7)	(17.3)	60.1	14.5	15.0
Other non-current assets	21,533	22,376	24,318	28,118	30,271		, ,	. ,			
Total assets	141,202	150,635	172,991	191,985	209,094	Profit & loss ratio (%)					
						Gross margin	37.2	31.6	35.3	35.2	35.2
Current liabilities	86,371	74,395	83,787	92,320	100,358	Operating margin	8.3	5.4	7.7	7.9	8.0
ST borrowings	27,258	12,664	15,990	16,680	16,312	Net profit margin	5.7	4.2	5.9	6.0	6.1
Account payables	18,356	17,152	22,036	22,232	27,707						
Tax payable	889	878	783	994	1,014	Balance sheet ratio					
Other current liabilities	39,868	43,701	44,978	52,414	55,325	Gearing ratio (%)	50	44	46	44	40
					·	Current ratio (x)	1.2	1.4	1.5	1.5	1.6
Non-current liabilities	16,877	30,117	36,571	39,016	39,000	Receivable turnover days	83	64	47	42	44
LT borrowings	10,045	22,614	28,555	29,787	29,129	Inventory turnover days	106	110	107	101	97
Deferred income	645	718	649	818	838	Payable turnover days	121	93	96	96	96
Other non-current liabilities	6,187	6,785	7,367	8,412	9,033						
Total liabilities	103,248	104,512	120,358	131,337	139,358	Profitability (%)					
						ROE	19.9	11.8	14.7	14.6	14.6
Shareholders' equity						ROA	3.6	2.8	3.9	4.1	4.3
Share capital	4,228	4,613	4,663	4,754	4,845						
Reserve	12,144	23,276	24,127	25,986	27,845	Per share data (RMB)					
Minority interest	2,875	2,826	3,101	3,521	3,792	EPS (RMB)	1.22	0.92	1.46	1.64	1.85
Total equity	37,954	46,123	52,633	60,649	69,736	DPS (RMB)	0.20	0.20	0.32	0.36	0.41
Total liabilities and equity	141,202			191,986		BVPS (RMB)	8.30	9.39	10.62	12.02	13.61
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Source: Company data, CMBIS estimates



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