

Sinotruk (Hong Kong) (3808 HK)

Uncover the hidden profitability in 1H20 results

Sinotruk's net profit in 1H20 grew 16% YoY to RMB2.94bn. While the earnings growth looks weaker than expectation, it was due to a RMB1.2bn YoY increase in administrative expense which included a provision for early retirement plan (~RMB800mn) and higher R&D expense (~RMB400mn). We see this a strategic move to further enhance Sinotruk's competitiveness in future. On the positive side, truck sales volume in 1H20 is better than expectation. Most importantly, operating cash inflow in 1H20 surged 215% YoY to a record of RMB13.5bn, equivalent to 4.3x of the after tax profit, suggesting excellent working capital management. We revised up Sinotruk's earnings forecast in 2020E-22E by 2-6% (13-20% above consensus), mainly due to higher sales volume assumptions. Our TP is lifted to HK\$28.3, based on 6x 2020E EV/EBITDA (multiple unchanged). Maintain **BUY**.

- Key financials in 1H20.** Revenue grew 24% YoY to RMB42.8bn, driven by a 24% increase in truck revenue and a 49% increase in engine revenue. EBIT grew 13% YoY to RMB4bn, mainly dragged by an 81% YoY increase in administrative expense. Operating cash inflow reached 13.5bn. As result, as at end-Jun, financial assets (wealth management products) and net cash reached >RMB30bn, accounting for >50% of Sinotruk's latest market cap.
- Sales of engine and truck better than expectations.** Sales volume of HDT grew 27% YoY to 118k units, mainly driven by 43% YoY increase in China sales. In particular, gas-fueled HDT sales grew 54% YoY to 22k units. LDT sales volume grew 24% YoY to ~82k unit. Sales of engine grew 32% YoY to ~129k units, with in-house consumption ratio rising to 95% in 1H20 from 93% in 1H19. Segment margin of LDT in 1H20 sharply recovered to 5.1% from -1.9% in 1H19, thanks to a sharp reduction on the impairment loss.
- Streamlining the labour force implies further cost reduction in future.** Sinotruk has been streamlining the labour force since 2018. Over the past two years, the number of staff engaging in R&D, sales & marketing were on the rise while production & administrative staff reduced (figure 2). In 1H20, total labour force reduced by 9% versus that in 2019, a key reason that Sinotruk recognized ~RMB800mn expense on termination and retirement benefits in 1H20 (based on our calculation). We believe this is one-off in nature and such move will reduce the staff cost over the coming years.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	61,785	62,227	76,986	80,381	82,579
YoY growth (%)	11.4	0.7	23.7	4.4	2.7
Net profit (RMB mn)	4,345	3,334	5,641	6,019	6,195
EPS (RMB)	1.51	1.14	2.04	2.18	2.24
YoY growth (%)	50.0	(24.6)	80.0	6.7	2.9
Consensus EPS (RMB)	N/A	N/A	1.76	1.77	1.78
P/E (x)	12.6	17.4	9.7	9.1	8.8
EV/EBITDA (x)	5.9	6.3	4.3	4.1	4.0
P/B (x)	2.1	2.0	1.7	1.5	1.4
Yield (%)	3.0	2.0	3.6	3.9	4.0
ROE (%)	18.0	12.6	19.1	17.8	16.3
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

Target Price	HK\$28.30
(Previous TP)	HK\$26.00)
Up/Downside	+29%
Current Price	HK\$21.95

China Capital Goods

Wayne Fung, CFA

(852) 3900 0826

waynefung@cmbi.com.hk

Stock Data

Mkt Cap (HK\$ mn)	60,604
Avg 3 mths t/o (HK\$ mn)	67
52w High/Low (HK\$)	25.55/10.96
Total Issued Shares (mn)	2,761

Source: Bloomberg

Shareholding Structure

CNHTC	51%
MAN SE	25%
Others	24%

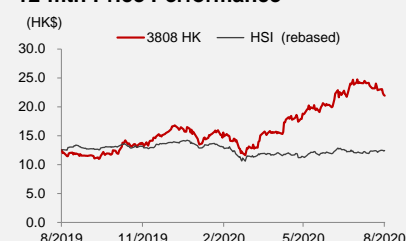
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-8.7%	-11.1%
3-mth	17.3%	8.1%
6-mth	41.8%	50.3%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: PWC

Related Reports

- China Construction Machinery & HDT Sector – Raise industry sales forecast in 2020E-21E; Solid upcycle – 30 Jun 2020
- Sinotruk (3808 HK, BUY) – Returning to growth territory in 2020E – 2 Apr 2020
- Sinotruk (3808 HK, BUY) – Incrementally positive on the back of more signs of recovery – 11 Mar 2020
- Sinotruk (3808 HK, BUY) – SHIG to officially control Sinotruk after the equity transfer – 30 Sep 2019

Figure 1: Highlights on 1H20 results

	1H19	1H20	Change (YoY)	Note
Sales volume (unit)	(Restated)			
Truck	158,576	199,955	26.1%	
HDT	92,668	118,073	27.4%	Strong HDT sales were driven by China market
China	72,706	104,181	43.3%	Included gas truck volume of 22k units (+54% YoY)
Export	19,962	13,892	-30.4%	
LDT	65,908	81,882	24.2%	Strong LDT growth helped by low base effect
Total	158,576	199,955	26.1%	
Engine	97,632	128,680	31.8%	Engine sales growth better than expectation
Internal use	90,700	122,246	34.8%	
External sales	6,932	6,434	-7.2%	
% of total				
Internal use	92.9%	95.0%		
External sales	7.1%	5.0%		
ASP (RMB/unit)				
Truck	216,024	212,543	-1.6%	
HDT	303,706	301,631	-0.7%	
LDT	92,741	84,078	-9.3%	
Engines	77,592	87,807	13.2%	Consistent increase in engine ASP
(RMB mn)				
Segment revenue				
Truck	34,256	42,499	24.1%	
HDT	28,144	35,614	26.5%	
LDT	6,112	6,885	12.6%	
Engine	7,575	11,299	49.2%	High growth driven by both volume & ASP
Finance	781	820	5.0%	
Intersegment sales	-7,990	-11,820	47.9%	
Total	34,623	42,798	23.6%	
Segment operating profit (before unallocated exp)				
Truck	1,829	2,625	43.6%	
HDT	1,946	2,277	17.0%	
LDT	-117	348	n/a	
Engine	1,255	1,749	39.4%	
Finance	458	426	-7.0%	
Intersegment sales	20	-786	n/a	
Total	3,561	4,014	12.7%	
Segment operating margin			Change (ppt)	
Truck	5.3%	6.2%	0.84	
HDT	6.9%	6.4%	-0.52	
LDT	-1.9%	5.1%	6.98	Driven by sharp decline in impairment & strong sales volume
Engine and gearbox	16.6%	15.5%	-1.09	The decrease was due to increase in R&D expenses, warranty expenses, provision for early retirement & termination plan.
Finance	58.6%	51.9%	-6.66	
Average	10.3%	9.4%	-0.91	
(RMB mn)				
Revenue	34,623	42,798	23.6%	
Cost of sales	(27,737.7)	(34,223.1)	23.4%	
Gross profit	6,886	8,575	24.5%	Gross margin expansion due to economies of scale & cost control
Other gains and losses	193.7	395.4	104.1%	
S&D expenses	(1,637.5)	(1,865.3)	13.9%	S&D expense ratio dropped 0.4ppt YoY to 4.4%
Administrative expenses	(1,530.6)	(2,762.3)	80.5%	Due to rising R&D & provision for employee termination benefits
Net impairment losses of financial assets	(353.9)	(334.4)	-5.5%	
EBIT	3,557	4,009	12.7%	
D&A	818	886	8.3%	
EBITDA	4,376	4,895	11.9%	
Net finance cost	-58	41	n/a	
Finance income	33	63	87.8%	
Finance expenses	-92	-22	-76.3%	
Share of profit of JV and associates	25	29	14.6%	
Pretax profit	3,524	4,079	15.7%	
Income tax	-767	-960	25.2%	
After tax profit	2,757	3,119	13.1%	
MI	-221	-177	-19.9%	
Net profit	2,536	2,941	16.0%	Core profit would be significant higher excluding the one-off provision for early retirement & termination plan

Source: Company data, CMBIS

Figure 2: Change in the number of staff

Number of staff					Change	
Function	2017	2018	2019	1H20	vs 2019	vs 2017
Management team	225	214	235	252	7%	12%
Technical	2,500	2,736	2,805	2,574	-8%	3%
R&D	910	1,008	1,129	1,507	33%	66%
Production	15,343	15,440	15,161	13,407	-12%	-13%
Sales	1,628	1,600	1,816	2,467	36%	52%
Marketing	210	220	412	357	-13%	70%
Administrative	4,003	3,930	3,904	2,583	-34%	-35%
Total	24,819	25,148	25,462	23,147	-9%	-7%

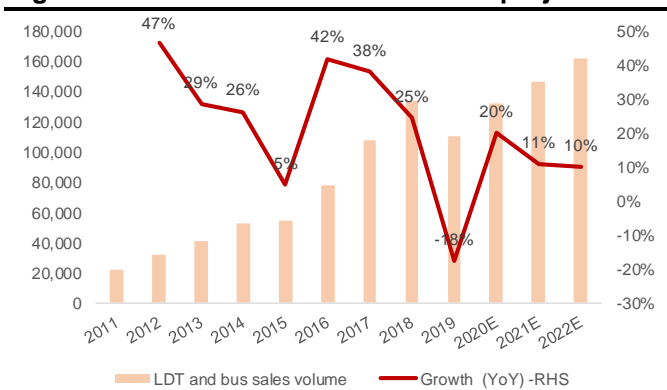
Source: Company data, CMBIS

Figure 3: Change in key operating assumptions

Sales volume (units)	2020			2021			2022		
	Old	New	Diff	Old	New	Diff	Old	New	Diff
Truck	305,583	336,020	10.0%	325,867	358,191	9.9%	343,104	376,593	9.8%
HDT	184,070	203,459	10.5%	189,772	211,049	11.2%	193,399	214,737	11.0%
China	143,661	168,251	17.1%	146,534	171,616	17.1%	147,999	173,332	17.1%
Export	40,409	35,208	-12.9%	43,238	39,433	-8.8%	45,400	41,405	-8.8%
LDT	121,514	132,560	9.1%	136,095	147,142	8.1%	149,705	161,856	8.1%
Engine	188,634	227,970	20.9%	192,257	232,382	20.9%	194,180	234,706	20.9%
Internal use	173,730	213,214	22.7%	177,204	217,478	22.7%	178,976	219,653	22.7%
External sales	14,904	14,757	-1.0%	15,053	14,904	-1.0%	15,204	15,053	-1.0%
Segment revenue									
(RMB mn)									
Truck	66,853	73,733	10.3%	69,927	77,377	10.7%	72,284	79,855	10.5%
HDT	55,589	61,445	10.5%	57,311	63,737	11.2%	58,406	64,851	11.0%
LDT	11,264	12,288	9.1%	12,616	13,640	8.1%	13,878	15,004	8.1%
Engine	16,279	20,833	28.0%	16,773	21,417	27.7%	16,979	21,669	27.6%
Finance	1,666	1,666	0.0%	1,683	1,683	0.0%	1,700	1,700	0.0%
Intersegment sales	-15,688	-19,246	22.7%	-16,351	-20,095	22.9%	-16,828	-20,645	22.7%
Total	69,111	76,986	11.4%	72,032	80,381	11.6%	74,134	82,579	11.4%
Segment operating margin									
Truck	6.0%	6.1%	0.1	6.0%	6.2%	0.2	6.0%	6.2%	0.2
HDT	6.9%	6.3%	(0.6)	6.9%	6.4%	(0.5)	6.9%	6.4%	(0.5)
LDT	1.7%	5.1%	3.4	2.0%	5.3%	3.3	2.2%	5.3%	3.1
Engine and gearbox	13.4%	14.0%	0.6	13.4%	14.3%	0.9	13.4%	14.5%	1.1
Finance	57.0%	50.5%	(6.5)	56.0%	50.0%	(6.0)	56.0%	50.0%	(6.0)
Average	10.3%	10.0%	(0.3)	10.2%	10.1%	(0.1)	10.2%	10.1%	(0.1)

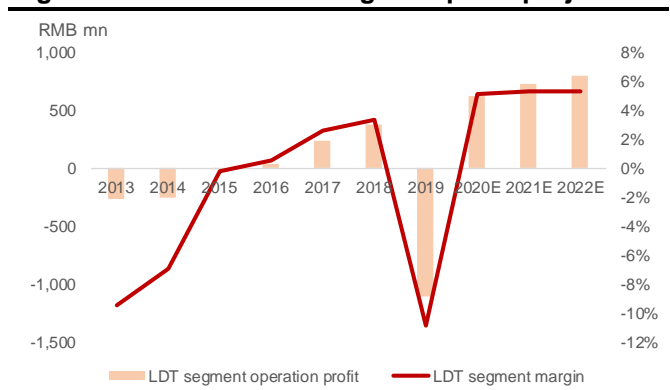
Source: Company data, CMBIS estimates

Figure 4: Sinotruk's LDT sales volume projection



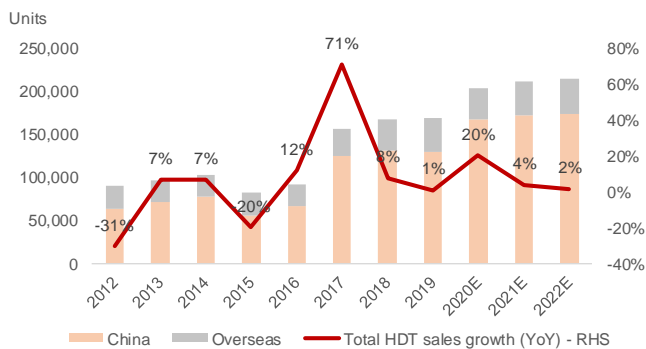
Source: Company data, CMBIS estimates

Figure 5: Sinotruk's LDT segment profit projection



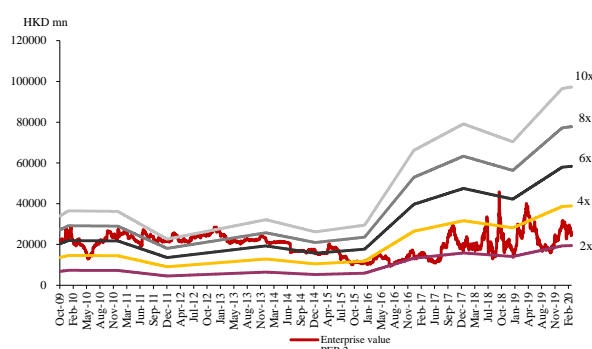
Source: Company data, CMBIS estimates

Figure 6: Sinotruk's HDT sales volume projection



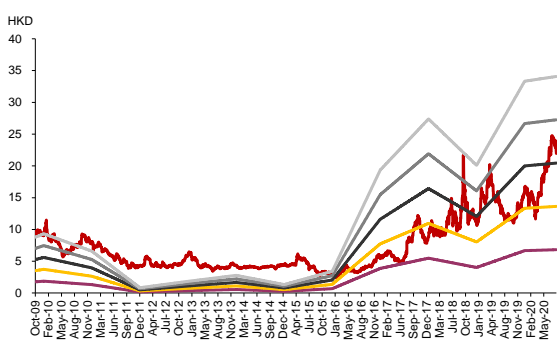
Source: Company data, CMBIS estimates

Figure 7: Sinotruk's EV/EBITDA band



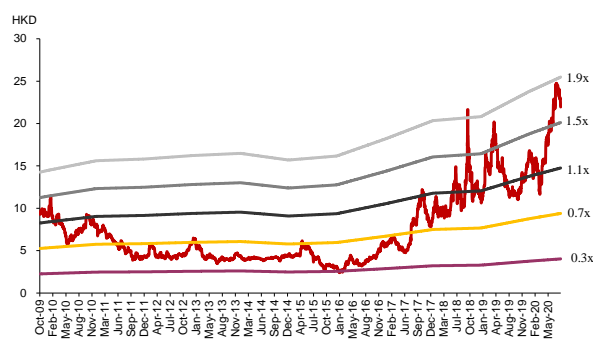
Source: Bloomberg, Company data, CMBIS estimates

Figure 8: Sinotruk P/E band



Source: Bloomberg, Company data, CMBIS estimates

Figure 9: Sinotruk P/B band



Source: Bloomberg, Company data, CMBIS estimates

- **Major risk factors:** (1) Slower-than-expected recovery of construction activities, and (2) increase in component cost.

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	61,785	62,227	76,986	80,381	82,579
Cost of sales	-50,610	-50,380	-61,974	-64,707	-66,476
Gross profit	11,175	11,847	15,012	15,674	16,103
Operating expenses	-5,532	-7,007	-7,349	-7,587	-7,801
EBIT	5,642	4,839	7,663	8,087	8,302
Net finance cost	-0	-96	51	82	103
Finance income	89	45	69	92	110
Finance expenses	-89	-141	-18	-10	-7
Profit of JV and associates	77	61	80	60	65
Pretax profit	5,719	4,805	7,793	8,229	8,470
Income tax	-993	-1,029	-1,792	-1,893	-1,948
After tax profit	4,726	3,776	6,001	6,336	6,522
MI	-381	-442	-360	-317	-326
Net profit	4,345	3,334	5,641	6,019	6,195
D&A	1,180	1,562	1,697	1,822	1,884
EBITDA	6,823	6,401	9,360	9,909	10,186

Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Pretax profit	5,719	4,805	7,793	8,229	8,470
Finance cost	89	141	18	10	7
Interest income	-89	-45	-69	-92	-110
Share of profit or loss of associates	-77	-61	-80	-60	-65
Depreciation	1,078	1,495	1,622	1,747	1,809
Amortization of intangible assets	102	67	75	75	75
Income tax paid	-1,043	-1,029	-1,792	-1,893	-1,948
Change in working capital	-1,639	1,853	6,935	1,404	958
Others	232	1,551	0	0	0
Cash flow from operation	4,374	8,775	14,503	9,420	9,196
Net capex on PP&E	-1,343	-1,034	-2,000	-1,600	-800
Dividend received	0	6	8	6	7
Interest received	89	45	69	92	110
Others	2,223	1,190	0	0	0
Cash flow from investing	979	-29	-3,316	-1,502	-683
Proceeds from equity financing	0	0	0	0	0
Net bank borrowings	-990	-2,000	-500	-200	0
Dividend paid	-1,615	-1,555	-1,077	-1,974	-2,107
Interest paid	-143	-141	-18	-10	-7
Others	117	-2,153	0	0	0
Cash flow from financing	-2,630	-5,849	-1,595	-2,184	-2,114
Change in cash	2,723	2,897	9,592	5,734	6,398
Cash at beginning of the year	9,840	12,616	17,931	27,523	33,256
Exchange gains/(losses) and others	53	2,418	0	0	0
Cash at end of the year	12,616	17,931	27,523	33,256	39,655

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	17,373	17,741	19,508	19,340	18,315
PP&E	10,366	9,906	10,824	10,677	9,668
Land use right	1,612	1,629	1,629	1,629	1,629
Investment in JV/associates	534	497	568	622	681
Investment properties	713	797	797	797	797
Long term receivables	2,195	2,907	2,907	2,907	2,907
Intangible assets	324	279	204	129	54
AFS / financial assets	212	0	0	0	0
Others	1,417	1,727	2,579	2,579	2,579
Current assets	44,308	48,210	66,061	65,732	78,254
Inventories	11,594	9,721	15,069	10,814	15,048
Trade and bills receivables	12,589	16,051	18,962	17,154	19,045
AFS / financial assets	4,601	1,715	1,715	1,715	1,715
Others	554	2,532	2,532	2,532	2,532
Restricted cash	2,352	260	260	260	260
Cash	12,616	17,931	27,523	33,256	39,655
Current liabilities	32,986	35,175	49,870	45,011	52,093
Trade and bills payables	28,305	31,455	46,649	41,991	49,072
Bank borrowings	3,000	1,000	500	300	300
Provisions	929	1,219	1,219	1,219	1,219
Others	752	1,501	1,501	1,501	1,501
Non-current liabilities	367	347	347	347	347
Bank borrowings	0	0	0	0	0
Deferred income	316	286	286	286	286
Others	50	62	62	62	62
Equity	28,328	30,428	35,352	39,714	44,129
Shareholders' equity	25,476	27,261	31,825	35,870	39,959
MI	2,852	3,167	3,527	3,844	4,170

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue mix (%)					
HDT	79.0	82.1	79.8	79.3	78.5
LDT & bus	18.5	16.4	16.0	17.0	18.2
Engine & gearbox	22.8	23.6	27.1	26.6	26.2
Finance	2.3	2.5	2.2	2.1	2.1
Intersegment sales	(22.6)	(24.6)	(25.0)	(25.0)	(25.0)
Total	100.0	100.0	100.0	100.0	100.0
Profit & loss ratio (%)					
Gross margin	18.1	19.0	19.5	19.5	19.5
EBIT margin	9.1	7.8	10.0	10.1	10.1
Net profit margin	7.6	6.1	7.8	7.9	7.9
Growth (%)					
Revenue	11.4	0.7	23.7	4.4	2.7
Gross profit	11.4	6.0	26.7	4.4	2.7
EBIT	32.1	-14.2	58.4	5.5	2.7
Net profit	43.7	-23.3	69.2	6.7	2.9
Core net profit	50.0	-24.6	80.0	6.7	2.9
Balance sheet ratio					
Current ratio (x)	1.3	1.4	1.3	1.5	1.5
Receivable turnover days	82	84	83	82	80
Inventory turnover days	90	77	73	73	71
Payable turnover days	205	216	230	250	250
Net debt / total equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Profitability (%)					
ROA	7.7	5.9	7.9	7.4	7.2
ROE	18.0	12.6	19.1	17.8	16.3
Per share data					
EPS (RMB)	1.57	1.21	2.04	2.18	2.24
Core EPS (RMB)	1.51	1.14	2.04	2.18	2.24
BVPS (RMB)	9.23	9.87	11.53	12.99	14.47
DPS (RMB)	0.56	0.39	0.72	0.76	0.79

Source: Company data, CMBIS estimates

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CMB International Securities Limited

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

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