

Shennan Circuits (002916 CH)

3Q could be lower despite satisfactory 2Q results

Shennan Circuits' 2Q22 revenue/NP to shareholders grew 15.8%/33.1% YoY and 10.3%/16.2% QoQ. GPM stabilized at 26%+ (vs. 22.5%-24.6% for 1Q21-4Q21), benefiting from easing material cost pressure and product structure adjustment. For 2022, Prismark forecasts PCB market to grow 4.2% YoY, moderate growth after significant growth of 24.1% YoY in 2021. Again, substrate market will lead the growth. For Shennan, we expect the PCB/substrate sales to grow 8.8%/18.9% respectively, driven by capacity ramp up and growing demand from auto markets. Total revenue growth is estimated at 7.7% for 2022. Overall, we think the Company will continue to face challenges, such as 1) slowdown of domestic 5G telecom capex, 2) delayed upgrade for Eagle stream platform, 3) soft consumer demand. We maintain HOLD and lower our TP to RMB96.6.

- **Although auto PCB capacity is ramping up and segment margin improves, PCB segment outlook remains cautious.** PCB sales grew 19.6% YoY in 2Q, due to growing demand from telecom (mainly overseas), datacenter and auto electronics markets. As Nantong phase III factory is ramping up capacity, we believe auto PCB sales will deliver decent growth this year. Meanwhile, material price is declining from the peak, which helps Shennan's PCB GPM improve to 27.3% in 1H22 (vs. 24.8% in 2H21). However, we maintain our cautious outlook, given detailed timeline of 5G deployment and upgrade of new datacenter platform is still unclear. Although the strong growth from auto PCB could partially offset these impacts, its revenue contribution is still insignificant (est. <5% in 2021).
- **Substrate demand weakening and supply chain constraint is easing.** Substrate sales grew 24.8% YoY in 1H22, mainly driven by new capacity released from Wuxi Phase II factory. The results was solid, after a good year for substrate in 2021 (segment rev. growth of 56.3% YoY). However, we think the unbalanced supply/demand situation is improving as consumer demand is weakening.
- **Maintain HOLD and lower TP to RMB96.6** We think Shennan is doing its best to navigate through macro uncertainties. However, we maintain our cautious outlook for PCB segment and lowered our FY22/23E EPS forecasts by 9%/12%. TP cut to RMB96.6, equal to 23x FY23E P/E, ~1SD below avg. 2-yr historical forward P/E. Potential upside: 1) stronger recovery in consumer demand, 2) resumed 5G deployment and Eagle steam platform upgrade.

Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Turnover (RMB mn)	11,600	13,943	15,017	17,417	20,066
YoY growth (%)	10.2%	20.2%	7.7%	16.0%	15.2%
Gross margin (%)	26.5%	23.7%	26.3%	26.1%	26.2%
Net profit (RMB mn)	1,430	1,481	1,730	2,055	2,411
EPS (RMB)	3.00	3.02	3.54	4.20	4.93
YoY growth (%)	-18.0%	0.7%	17.1%	18.8%	17.3%
Consensus EPS (RMB)	NA	NA	3.63	4.35	0.00
PE (x)	31.3	31.1	26.5	22.3	19.0
Yield (%)	0.0%	1.0%	1.0%	1.0%	1.7%
ROE (%)	19.2%	17.4%	14.1%	15.0%	15.6%
Net gearing (%)	10.5%	12.9%	Net cash	1.2%	Net cash

Source: Company data, Bloomberg, CMBIGM estimates

HOLD (Maintain)

Target Price	RMB96.60
(Previous TP	RMB102.00)
Up/Downside	+2.6%
Current Price	RMB 94.17

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Stock Data

Mkt Cap (HK\$ mn)	48,298
Avg 3 mths t/o (HK\$ mn)	245
52w High/Low (HK\$)	123.74/84.8
Total Issued Shares (mn)	512.9

Source: Bloomberg

Shareholding Structure

AVIC International Holdings	63.97%
HK Securities Clearing	2.69%
China Asset Management Co	0.85%

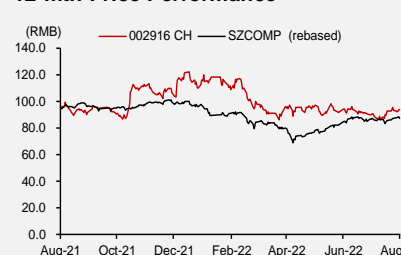
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	4.0%	1.9%
3-mth	-2.1%	-15.0%
6-mth	-13.7%	-10.8%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: BDO

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Earnings Review

Figure 1: Quarterly results

RMB mn	1Q21	2Q21	3Q21	4Q21	1Q22	2Q22	QoQ	YoY
Revenue	2,725	3,156	3,875	4,187	3,316	3,656	10.3%	15.8%
Gross Profit	639	772	951	943	888	958	7.9%	24.1%
Operating Profit	277	337	509	494	380	439	15.6%	30.5%
Net profit	244	304	473	460	348	404	16.2%	33.1%
EPS (RMB)	0.50	0.64	0.95	0.93	0.70	0.79	12.9%	23.4%
Gross Margin	23.4%	24.5%	24.6%	22.5%	26.8%	26.2%	-0.6 ppt	1.7 ppt
Operating Margin	10.2%	10.7%	13.1%	11.8%	11.5%	12.0%	0.6 ppt	1.4 ppt
Net Margin	8.9%	9.6%	12.2%	11.0%	10.5%	11.1%	0.6 ppt	1.4 ppt

Source: Company data, CMBIGM estimate

Figure 2: Earnings revision

	New			Old			Diff (%)		
US\$ mn	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	15,017	17,417	20,066	16,496	19,399	23,080	-9%	-10%	-13%
Gross Profit	3,944	4,554	5,267	4,110	4,948	6,090	-4%	-8%	-14%
Operating Profit	1,885	2,242	2,630	2,102	2,571	3,373	-10%	-13%	-22%
Net profit	1,730	2,055	2,411	1,906	2,337	3,064	-9%	-12%	-21%
EPS (US\$ cents)	3.54	4.20	4.93	3.90	4.78	6.26	-9%	-12%	-21%
Gross Margin	26.3%	26.1%	26.2%	24.9%	25.5%	26.4%	1.4 ppt	0.6 ppt	-0.1 ppt
Operating Margin	12.6%	12.9%	13.1%	12.7%	13.3%	14.6%	-0.2 ppt	-0.4 ppt	-1.5 ppt
Net Margin	11.5%	11.8%	12.0%	11.6%	12.0%	13.3%	0 ppt	-0.2 ppt	-1.3 ppt

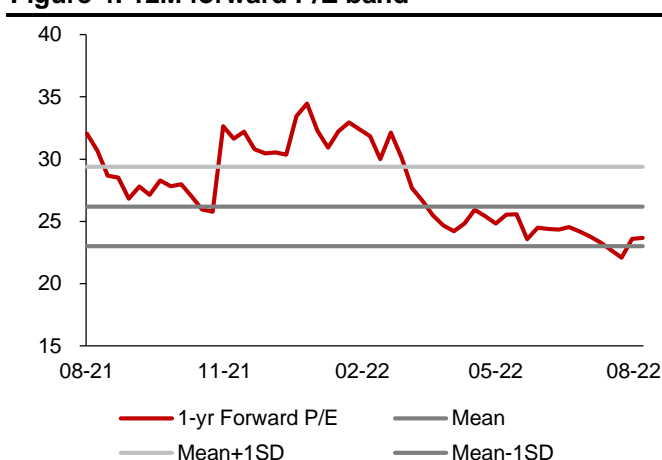
Source: Company data, CMBIGM estimates

Figure 3: CMBIGM estimates vs consensus

US\$ mn	CMBIGM			Consensus			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	15,017	17,417	20,066	16,314	19,215	22,396	-8%	-9%	-10%
Gross Profit	3,944	4,554	5,267	4,009	4,742	5,574	-2%	-4%	-6%
Operating Profit	1,885	2,242	2,630	2,120	2,541	3,069	-11%	-12%	-14%
Net profit	1,730	2,055	2,411	1,832	2,232	2,674	-6%	-8%	-10%
EPS (US\$ cents)	3.54	4.20	4.93	3.63	4.35	5.20	-3%	-3%	-5%
Gross Margin	26.3%	26.1%	26.2%	24.6%	24.7%	24.9%	1.7 ppt	1.5 ppt	1.4 ppt
Operating Margin	12.6%	12.9%	13.1%	13.0%	13.2%	13.7%	-0.4 ppt	-0.3 ppt	-0.6 ppt
Net Margin	11.5%	11.8%	12.0%	11.2%	11.6%	11.9%	0.3 ppt	0.2 ppt	0.1 ppt

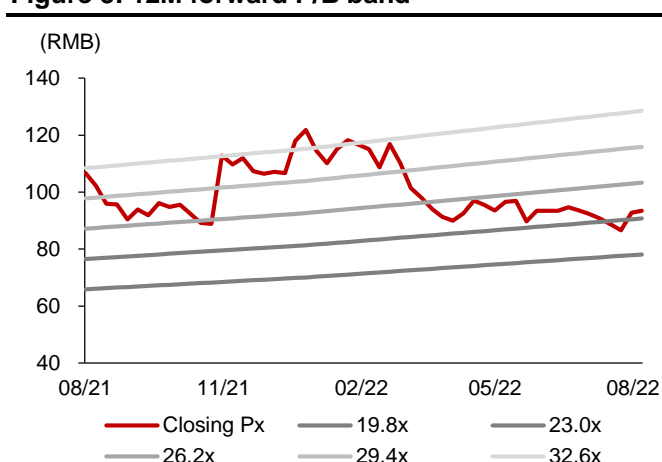
Source: Company data, CMBIGM estimates

Figure 4: 12M forward P/E band



Source: Company data, CMBIGM estimates

Figure 5: 12M forward P/B band



Source: Company data, CMBIGM estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	11,600	13,943	15,017	17,417	20,066
Cost of sales	(8,530)	(10,637)	(11,073)	(12,863)	(14,799)
Gross profit	3,071	3,306	3,944	4,554	5,267
Selling exp	(167)	(233)	(263)	(305)	(351)
Admin exp (excl. R&D)	(480)	(543)	(680)	(771)	(868)
R&D exp	(645)	(782)	(857)	(994)	(1,145)
Finance costs	(152)	(107)	(106)	(113)	(120)
Other operating exp.	2,889	3,354	3,965	4,495	5,122
Operating profit	1,625	1,617	1,885	2,242	2,630
Other non-oper exp.	(19)	(8)	(4)	(7)	(7)
Pre-tax profit	1,606	1,609	1,882	2,235	2,623
Income tax expense	(175)	(128)	(151)	(180)	(211)
Minority interests	1	0	0	0	1
Net profit	1,430	1,481	1,730	2,055	2,411

Cash flow

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Net profit	1,431	1,481	1,730	2,055	2,412
D&A	591	793	928	1,080	1,263
Change in working capital	(557)	(363)	(866)	252	(670)
Others	335	431	552	(669)	1,116
Net cash from operating	1,800	2,342	2,344	2,718	4,122
Capex	(2,486)	(2,658)	(2,195)	(2,487)	(2,745)
Other	(149)	178	(1,023)	159	209
Net cash from investing	(2,635)	(2,481)	(3,217)	(2,328)	(2,536)
Share issuance	0	0	2,500	0	0
Dividend paid	(453)	(541)	(602)	(693)	(808)
Other	383	802	(84)	(153)	(144)
Net cash from financing	(71)	261	1,814	(846)	(952)
Net change in cash	(905)	122	941	(455)	634
Cash at beginning of the year	1,441	504	620	1,560	1,105
Exchange difference	9	(31)	0	0	0
Cash at the end of the year	504	620	1,560	1,105	1,739

Balance sheet

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Current assets	5,941	7,270	9,599	10,695	11,461
Cash & equivalents	507	620	1,562	1,106	1,740
Account receivables	2,053	2,732	3,111	3,266	3,881
Inventory	2,206	2,527	2,873	3,125	3,606
Prepayment	6	16	26	22	30
Other current assets	1,169	1,377	2,026	3,177	2,203
Non-current assets	8,067	9,522	11,010	12,592	14,226
PPE	6,485	7,789	8,595	9,816	11,143
Deferred tax assets	72	91	110	125	137
Other non-current	1,509	1,642	2,306	2,650	2,946
Total assets	14,008	16,792	20,609	23,287	25,687
Current liabilities	4,932	5,948	6,885	7,851	8,251
ST borrowings	232	350	80	73	17
Account payables	1,515	1,881	2,063	2,281	2,423
Tax payable	22	78	45	79	72
Other current liabilities	3,163	3,639	4,697	5,419	5,739
Non-current liabilities	1,631	2,325	1,461	1,686	1,951
LT borrowings	1,059	1,368	1,036	1,199	1,418
Deferred tax liability	6	7	74	47	72
Other non-current	566	950	350	441	461
Total liabilities	6,563	8,272	8,345	9,537	10,202
Share capital	489	489	489	489	489
Reserve	3,660	3,675	6,175	6,175	6,175
Retained earnings	3,135	4,150	5,393	6,879	8,614
Other	158	202	202	202	202
Minority interest	3	3	4	4	4
Total equity	7,444	8,520	12,263	13,749	15,485
Total liabilities and equity	14,008	16,792	20,609	23,287	25,687

Key ratios

YE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue mix					
PCB	8,311	8,737	9,506	10,856	10,656
PCBA	1,160	1,940	1,700	1,839	1,926
Substrate	1,544	2,415	2,875	3,693	6,352
Growth (%)					
Revenue	10.2%	20.2%	7.7%	16.0%	15.2%
Gross profit	10.0%	7.6%	19.3%	15.5%	15.7%
Operating profit	14.7%	-0.5%	16.6%	18.9%	17.3%
Net profit	16.0%	3.5%	16.8%	18.8%	17.3%
Profit & loss ratio (%)					
Gross margin	26.5%	23.7%	26.3%	26.1%	26.2%
Operating margin	14.0%	11.6%	12.6%	12.9%	13.1%
Net profit margin	12.3%	10.6%	11.5%	11.8%	12.0%
Balance sheet ratio					
Net debt/total equity (%)	10.5%	12.9%	Net	1.2%	Net
Current ratio (x)	1.2	1.2	1.4	1.4	1.4
Receivable turnover days	65	63	71	67	65
Inventory turnover days	(79)	(81)	(89)	(85)	(83)
Payable turnover days	(66)	(58)	(65)	(62)	(58)
Profitability (%)					
ROE	19.2%	17.4%	14.1%	15.0%	15.6%
ROA	10.2%	8.8%	8.4%	8.8%	9.4%
Per share data (RMB)					
EPS	3.00	3.02	3.54	4.20	4.93
DPS	0.00	0.95	0.95	0.95	1.62
BPS	15.61	17.41	25.06	28.10	31.64

Source: Company data, CMBIGM estimates

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