ZTE (763 HK)

Compute growth accelerates but margin pressure persists

ZTE reported 1H26 results with revenue up 9.1% YoY to RMB78.0bn, while net profit fell 45.6% YoY to RMB2.75bn. In 2Q26, revenue increased 11.5% YoY and 23.0% QoQ to RMB43.0bn, above Bloomberg consensus, while net profit declined 44.6% YoY but rose 10.1% QoQ to RMB1.44bn. Computing revenue grew over 55% YoY and accounted for 35.1% of total sales, with server and storage revenue up nearly 60% and datacenter sales up 90%+. 1H26 GPM fell 7.0ppts YoY to 25.5%, mainly due to lower carrier revenue and a shift towards lower-margin E&G sales. Looking ahead, we remain positive on top-line growth as AI server and datacenter sales continue to expand, supported by robust overseas demand. However, the evolving revenue mix and weak domestic telco spending will likely keep margins under pressure. **Maintain BUY** as ZTE's rapidly scaling AI infra. business should sustain revenue growth. **TP is adjusted to HK$35.5, based on 22x 2027E P/E (previously HK$38.6 based on 25x 2026E P/E), broadly in line with peers.**

- **Revenue mix transition continues to weigh on margins.** Carrier revenue declined 9.4% YoY to RMB31.8bn in 1H26 as domestic 5G investment remained weak, partly offset by growth in overseas carrier markets. Segment GPM fell sharply by 14.9ppts YoY to 38.1%, reflecting an unfavourable product mix and heightened pricing competition. Carrier revenue accounted for 40.7% of total sales, down from 49.0% in 1H25. We expect domestic carrier demand to remain subdued, while 5G deployments and fixed-network upgrades in emerging markets should provide some support.
- **Overseas markets remained resilient and should continue to support growth.** Overseas revenue grew 33.1% YoY to RMB27.9bn and accounted for 35.7% of total sales. Revenue increased 53.4% YoY in Asia excluding China, 48.6% in Africa and 10.9% in Europe, the Americas and Oceania. Growth was supported by overseas 5G and fixed-network upgrades, stronger computing-infrastructure demand and double-digit growth in international consumer products. We expect ZTE's overseas expansion to help offset subdued domestic carrier spending and support further market-share gains.
- **Maintain BUY with TP adjusted to HK$35.5, based on 22x 2027E P/E.** We slightly update our FY26/FY27E revenue forecasts by 0.2%/1.3%, while lowering our GPM forecasts by 3.6ppts/3.6ppts to reflect a higher mix of lower-margin computing sales**. Key risks:** Weak domestic telecom capex, AI infra. capex slowdown, unfavourable revenue mix, etc..

Earnings Summary

(YE 31 Dec)	FY24A	FY25A	FY26E	FY27E	FY28E
Revenue (RMB mn)	121,299	133,895	149,219	170,586	190,994
YoY growth (%)	(2.4)	10.4	11.4	14.3	12.0
Gross margin (%)	37.9	30.3	25.5	24.9	24.7
Net profit (RMB mn)	8,424.8	5,617.7	6,508.1	6,792.5	7,199.1
YoY growth (%)	(9.7)	(33.3)	15.8	4.4	6.0
EPS (Reported) (RMB)	1.76	1.17	1.36	1.42	1.50
P/E (x)	11.6	17.5	15.0	14.4	13.6
ROE (%)	12.0	7.6	8.4	8.3	8.3

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	**HK$35.50**
(Previous TP	HK$38.60)
Up/Downside	**48.8%**
Current Price	**HK$23.86**

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Stock Data

Mkt Cap (HK$ mn)	18,026.2
Avg 3 mths t/o (HK$ mn)	644.4
52w High/Low (HK$)	43.30/21.80
Total Issued Shares (mn)	755.5

Source: FactSet

Shareholding Structure

BlackRock	5.9%
Capital Group	5.7%

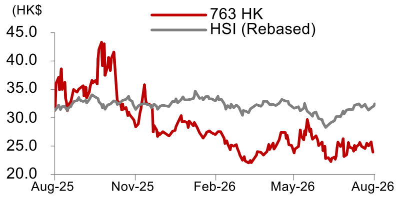
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	-2.2%	-5.5%
3-mth	0.3%	-2.1%
6-mth	-11.7%	-10.3%

Source: FactSet

12-mth Price Performance



Source: FactSet

Figure 1: Earnings revision

	New			Old			Diff (%)		
RMBmn	**FY26E**	**FY27E**	**FY28E**	**FY26E**	**FY27E**	**FY28E**	**FY26E**	**FY27E**	**FY28E**
Revenue	149,219	170,586	190,994	148,992	168,360	185,308	0.2%	1.3%	3.1%
Gross profit	38,092	42,514	47,225	43,357	47,983	53,183	-12.1%	-11.4%	-11.2%
Net profit	6,508	6,793	7,199	6,496	9,041	11,214	0.2%	-24.9%	-35.8%
EPS (RMB)	1.36	1.42	1.50	1.36	1.89	2.34	0.0%	-24.9%	-35.7%
Gross margin	25.5%	24.9%	24.7%	29.1%	28.5%	28.7%	-3.6 ppt	-3.6 ppt	-4 ppt
Net margin	4.4%	4.0%	3.8%	4.4%	5.4%	6.1%	0 ppt	-1.4 ppt	-2.3 ppt

Source: Company data, CMBIGM estimates

Figure 2: CMBIGM estimates vs. BBG consensus

	CMBI estimates			Consensus			Diff (%)		
RMBmn	**FY26E**	**FY27E**	**FY28E**	**FY26E**	**FY27E**	**FY28E**	**FY26E**	**FY27E**	**FY28E**
Revenue	149,219	170,586	190,994	148,469	165,071	189,302	0.5%	3.3%	0.9%
Gross profit	38,092	42,514	47,225	39,793	41,824	47,560	-4.3%	1.6%	-0.7%
Net profit	6,508	6,793	7,199	6,525	7,607	7,450	-0.3%	-10.7%	-3.4%
EPS (RMB)	1.36	1.42	1.50	1.37	1.60	1.57	-0.9%	-11.4%	-3.8%
Gross margin	25.5%	24.9%	24.7%	26.8%	25.3%	25.1%	-1.3 ppt	-0.4 ppt	-0.4 ppt
Net margin	4.4%	4.0%	3.8%	4.4%	4.6%	3.9%	0 ppt	-0.6 ppt	-0.2 ppt

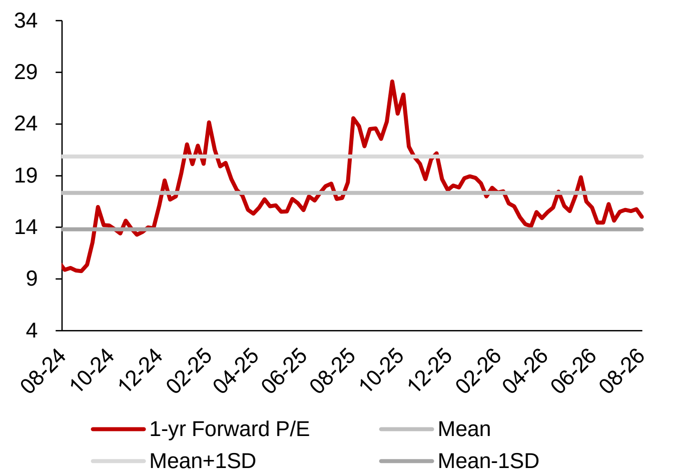
Source: Bloomberg consensus, CMBIGM estimates

Figure 3: Peers comparison

		Mkt Cap	P/E (x)		EPS (US$)		GPM%	
Company	**Ticker**	**(US$mn)**	**FY26E**	**FY27E**	**FY26E**	**FY27E**	**FY26E**	**FY27E**
IEIT Systems	000977 CH	12,658	23.3	18.5	0.37	0.46	6.5	6.6
Huaqin Tech	603296 CH	17,441	21.5	17.4	0.54	0.67	8.1	8.2
Fiberhome	600498 CH	8,223	27.0	18.5	0.22	0.32	26.1	27.5
Ruijie Network	301165 CH	9,807	45.2	33.7	0.27	0.37	33.5	32.9
		Average	***29.3***	***22.0***	***0.35***	***0.46***	***18.6***	***18.8***

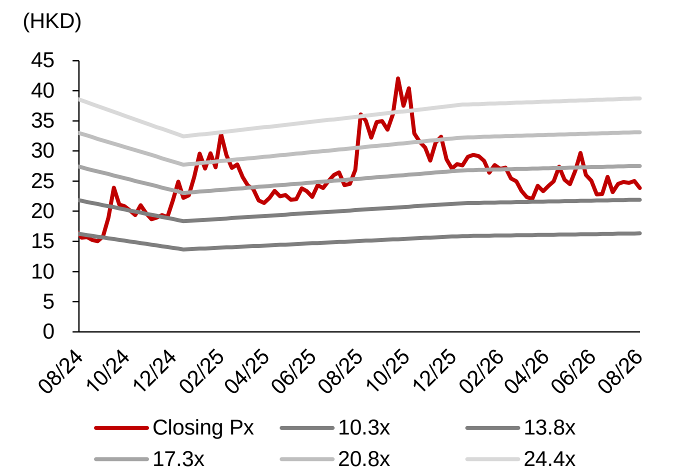
Source: Bloomberg consensus

Figure 4: P/E chart



Source: Company data, CMBIGM estimates

Figure 5: P/E band



Source: Company data, CMBIGM estimates

Financial Summary

INCOME STATEMENT	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec (RMB mn)						
Revenue	**124,251**	**121,299**	**133,895**	**149,219**	**170,586**	**190,994**
Cost of goods sold	(72,650)	(75,311)	(93,391)	(111,127)	(128,072)	(143,769)
Gross profit	**51,601**	**45,988**	**40,504**	**38,092**	**42,514**	**47,225**
Operating expenses	**(40,623)**	**(35,652)**	**(34,402)**	**(30,164)**	**(34,142)**	**(37,844)**
Selling expense	(10,172)	(8,901)	(9,223)	(7,461)	(8,188)	(8,786)
Admin expense	(5,632)	(4,477)	(4,220)	(3,581)	(4,094)	(4,584)
SG&A expense	(1,336)	(1,176)	(1,090)	(1,215)	(1,389)	(1,555)
R&D expense	(25,289)	(24,031)	(22,755)	(20,891)	(23,882)	(26,739)
Others	1,806	2,933	2,887	2,984	3,412	3,820
Operating profit	**10,978**	**10,335**	**6,102**	**7,928**	**8,372**	**9,380**
Other income	173	76	201	224	256	286
Other expense	(228)	(189)	(260)	(289)	(331)	(370)
Gain/loss on financial assets at FVTPL	(702)	(625)	102	102	102	102
Investment gain/loss	(205)	112	453	219	219	219
Other gains/(losses)	(914)	(745)	(521)	(547)	(529)	(553)
EBIT	**9,102**	**8,965**	**6,076**	**7,635**	**8,088**	**9,063**
Net Interest income/(expense)	**1,101**	**265**	**227**	**(283)**	**(366)**	**(905)**
Other income/expense	158	(687)	(375)	(375)	(375)	(375)
Pre-tax profit	**10,203**	**9,230**	**6,303**	**7,352**	**7,722**	**8,158**
Income tax	(962)	(874)	(738)	(778)	(861)	(887)
After tax profit	**9,241**	**8,356**	**5,565**	**6,574**	**6,861**	**7,272**
Minority interest	(85)	(69)	(53)	66	69	73
Others	0	0	0	0	0	0
Net profit	**9,326**	**8,425**	**5,618**	**6,508**	**6,793**	**7,199**

BALANCE SHEET	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec (RMB mn)						
Current assets	**158,505**	**141,787**	**143,934**	**150,000**	**132,344**	**162,594**
Cash & equivalents	51,013	28,027	25,482	16,465	13,409	7,475
Restricted cash	27,530	15,859	8,269	8,269	8,269	8,269
Account receivables	21,968	23,886	24,063	28,266	25,947	34,752
Inventories	41,131	41,258	47,017	57,717	48,952	70,791
Prepayment	242	692	1,443	882	1,185	1,228
Financial assets at FVTPL	153	13,769	17,396	17,995	16,259	19,343
Other current assets	16,466	18,297	20,263	20,405	18,323	20,737
Non-current assets	**42,454**	**65,536**	**73,806**	**75,231**	**71,161**	**79,506**
PP&E	14,360	14,178	13,422	12,679	11,750	11,057
Right-of-use assets	1,557	1,552	1,534	1,488	1,422	1,318
Deferred income tax	4,146	4,396	5,166	5,343	4,828	5,744
Intangibles	8,999	7,159	6,017	4,934	4,398	4,281
Goodwill	0	14	0	0	0	0
Financial assets at FVTPL	832	716	1,793	1,793	1,793	1,793
Other non-current assets	12,559	37,520	45,874	48,994	46,971	55,314
Total assets	**200,958**	**207,323**	**217,739**	**225,231**	**203,504**	**242,100**
Current liabilities	**83,030**	**82,635**	**81,981**	**108,176**	**83,676**	**115,708**
Short-term borrowings	7,560	7,027	3,629	5,507	(1,118)	(496)
Account payables	32,219	36,568	36,866	61,181	46,081	71,826
Tax payable	1,413	1,205	1,128	1,167	1,055	1,255
Other current liabilities	10,771	7,984	9,673	8,580	8,980	9,006
Contract liabilities	31,067	29,851	30,685	31,741	28,679	34,118
Non-current liabilities	**49,596**	**51,577**	**60,117**	**36,806**	**34,995**	**36,665**
Long-term borrowings	42,576	44,059	45,713	22,175	21,022	21,522
Bond payables	0	1,005	7,810	7,810	7,810	7,810
Obligations under finance leases	960	973	940	973	879	1,046
Deferred income	78	91	108	112	101	120
Other non-current liabilities	5,982	5,450	5,547	5,737	5,184	6,167
Total liabilities	**132,627**	**134,213**	**142,098**	**144,982**	**118,672**	**152,372**
Share capital	4,783	4,784	4,784	4,784	4,784	4,784
Capital surplus	0	0	0	0	0	0
Retained earnings	34,715	39,873	42,539	47,081	51,596	56,418
Other reserves	28,510	28,152	28,103	28,103	28,103	28,103
Total shareholders equity	**68,008**	**72,808**	**75,426**	**79,968**	**84,483**	**89,305**
Minority interest	323	302	216	281	350	423
Total equity and liabilities	**200,958**	**207,323**	**217,739**	**225,231**	**203,504**	**242,100**

CASH FLOW	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	**9,241**	**8,356**	**5,565**	**6,574**	**6,861**	**7,272**
Depreciation & amortization	4,926	4,969	4,758	5,114	5,386	5,727
Tax paid	(437)	(237)	(752)	(174)	505	(897)
Change in working capital	(324)	(2,505)	(7,017)	9,496	(4,175)	(4,828)
Others	3,999	898	1,365	4,922	1,004	5,616
Net cash from operations	**17,406**	**11,480**	**3,919**	**25,932**	**9,581**	**12,891**
Investing						
Capital expenditure	(4,005)	(4,015)	(3,893)	(5,966)	(6,401)	(7,277)
Acquisition of subsidiaries/ investments	(17,001)	(25,299)	(3,060)	(282)	2,065	(2,780)
Net proceeds from disposal of short-term investments	104	535	77	421	433	448
Others	(635)	(415)	(575)	(1,069)	3,101	(5,509)
Net cash from investing	**(21,536)**	**(29,193)**	**(7,451)**	**(6,896)**	**(801)**	**(15,119)**
Financing						
Dividend paid	(4,836)	(5,419)	(4,368)	(5,239)	(4,635)	(4,540)
Net borrowings	11,164	(253)	5,473	(22,814)	(7,201)	834
Proceeds from share issues	1,676	374	0	0	0	0
Others	(633)	(521)	(575)	0	0	0
Net cash from financing	**7,372**	**(5,818)**	**530**	**(28,053)**	**(11,835)**	**(3,706)**
Net change in cash						
Cash at the beginning of the year	47,072	51,013	28,027	25,482	16,465	13,409
Exchange difference	66	24	(117)	0	0	0
Others	3,876	(23,011)	(2,427)	(9,017)	(3,056)	(5,935)
Cash at the end of the year	**51,013**	**28,027**	**25,482**	**16,465**	**13,409**	**7,475**

GROWTH	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
Revenue	1.1%	(2.4%)	10.4%	11.4%	14.3%	12.0%
Gross profit	12.8%	(10.9%)	(11.9%)	(6.0%)	11.6%	11.1%
Operating profit	4.0%	(5.9%)	(41.0%)	29.9%	5.6%	12.0%
EBIT	2.1%	(1.5%)	(32.2%)	25.7%	5.9%	12.1%
Net profit	15.4%	(9.7%)	(33.3%)	15.8%	4.4%	6.0%

PROFITABILITY	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
Gross profit margin	41.5%	37.9%	30.3%	25.5%	24.9%	24.7%
Operating margin	8.8%	8.5%	4.6%	5.3%	4.9%	4.9%
Return on equity (ROE)	14.7%	12.0%	7.6%	8.4%	8.3%	8.3%

GEARING/LIQUIDITY/ACTIVITIES	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
Current ratio (x)	1.9	1.7	1.8	1.4	1.6	1.4

VALUATION	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
P/E	10.4	11.6	17.5	15.0	14.4	13.6
P/E (diluted)	10.4	11.6	17.6	15.0	14.4	13.6

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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