

# AAC Technologies (2018 HK)

## Awaiting better visibility in 2Q; Maintain SELL

We maintain Sell rating with lowered TP of HK\$35.8 for our cautious view on iPhone launch delay, aggressive optics guidance and order uncertainty. Although recent 40% share price correction has priced in 1H20 iPhone weakness and COVID-19 supply impact, we believe there is still downside on consensus earnings due to product launch delays and demand weakness. We trimmed FY20/21E EPS by 15%/7% for 4Q19 miss, weaker margin and COVID-19 disruption. Our EPS are 31%/26% are below consensus. We would take a more positive stance if we saw demand recovery, better lens shipment and gross margin improvement.

- 4Q19 miss on GPM and lower ASP.** AAC reported 4Q19 net profit decline of 27% YoY, 5%/24% below our/consensus estimates. The miss was mainly due to 1) weaker GPM in acoustics/haptics, and 2) optic's weaker ASP and lower shipment of 45kk/m in 4Q (vs 60kk/m prev. guidance). By segment, acoustics (42% of sales) reversed declining trend with 19% growth, while haptics/casings (46%) declined 6% YoY and optics (6%) grew 150% YoY.
- Conservative on optics's aggressive guidance.** Optics was the only bright spot in 4Q19 with 150% revenue YoY (vs 81% YoY in 3Q). Mgmt. targets to achieve 100kk/m plastic lens shipment (vs 45kk/m in 4Q19) with ASP Rmb 4.2-4.5 by Jul 2020 (delayed from 1Q20E), and 6P/7P shipment will start in 3Q20E. As for WLJ lens, mgmt. plans to start mass production in 2Q20E and annual shipment will reach 30mn in FY20E. While we are impressed by AAC's optics progress, we think shipment guidance of 100k/m by July looks too aggressive given Sunny's conservative view on handset lens and order uncertainty in 2H20E.
- Our FY20/21E EPS are 31%/26% below consensus.** After 7 consecutive quarters of earnings decline due to share loss and slow spec upgrade, we expect AAC's gross margin will remain under pressure in FY20E. We expect net profit to grow -0.1%/-2.4%/+6.4% YoY in 2Q/3Q/4Q20E, driven by 1) deteriorated landscape in acoustics/haptics market, 2) slower-than-expected optics ramp given Sunny's conservative shipment/ASP guidance, and 3) lack of major upgrade except optics (6% of AAC sales).
- Maintain Sell; demand visibility remains weak.** While market has priced in 1H20 weakness, we expect earnings downward revision and iPhone launch uncertainty due to COVID-19 will continue to put the stock under pressure. Our new TP of HK\$35.8 is based on same target multiple of 18x FY20E P/E. Upside risks include stronger lens, better iPhone and less margin pressure.

### Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	18,131	17,884	18,060	20,321	21,729
YoY growth (%)	(14.1)	(1.4)	1.0	12.5	6.9
Net income (RMB mn)	3,796	2,222	2,161	2,718	2,997
EPS (RMB)	3.12	1.84	1.79	2.25	2.48
YoY growth (%)	(28.5)	(41.1)	(2.8)	25.8	10.3
Consensus EPS (RMB)	NA	1.93	2.57	3.05	3.46
P/E (x)	11.6	19.6	20.2	16.1	14.6
P/B (x)	2.3	2.2	2.1	2.0	1.8
Yield (%)	5.0	3.5	3.4	2.2	2.4
ROE (%)	20.0	11.3	10.6	12.3	12.5

Source: Company data, Bloomberg, CMBIS estimates

### SELL (Maintain)

Target Price	HK\$35.8
(Previous TP)	HK\$45.0
Up/Downside	-11%
Current Price	HK\$40.2

### China Technology Sector

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#### Stock Data

Mkt. Cap. (HK\$m)	48,582
Avg. 3mths t/o (HK\$m)	369.45
52W High/Low (HK\$)	70/33.21
Total Issued Shares (mn)	1,209

Source: Bloomberg

#### Shareholding Structure

Chunyuan Wu	21.75%
Zhengmin Pan	19.24%
JPMorgan Chase	12.39%

Source: HKEx

#### Share Performance

	Absolute	Relative
1-mth	-29.5%	-12.5%
3-mth	-38.8%	-15.6%
6-mth	-4.1%	-9.3%

Source: Bloomberg

#### 12-mth Price Performance



Source: Bloomberg

#### Auditor: Deloitte Touche Tohmatsu

#### Related Reports:

- AAC Tech (2018 HK) – Worst is likely over but most positives are priced in – 11 Nov 2019
- AAC Tech (2018 HK) – Outlook remains challenging; Maintain Sell - 26 Aug 2019
- AAC Tech (2018 HK) – 1H Preview

## 4Q19 Results Review

Figure 1: 4Q19 results review

RMB mn	4Q18	3Q19	4Q19	QoQ	YoY	CMBI estimates		Consensus	
						4Q19E	Diff %	4Q19E	Diff %
Revenue	4,838	5,012	5,305	6%	10%	4,941	7%	5,493	-3%
Gross Profit	1,844	1,483	1,539	4%	-17%	1,523	1%	1,200	28%
Operating Profit	1,135	829	801	-3%	-29%	827	-3%	1,045	-23%
Net profit	1,044	695	757	9%	-27%	794	-5%	909	-17%
EPS (RMB)	0.85	0.57	0.63	9%	-27%	0.65	-4%	0.75	-16%
Gross Margin	38.1%	29.6%	29.0%			30.8%	-1.8 ppt	32.0%	-3 ppt
Operating Margin	23.5%	16.5%	15.1%			16.7%	-1.6 ppt	19.0%	-3.9 ppt
Net Margin	21.6%	13.9%	14.3%			16.1%	-1.8 ppt	16.6%	-2.3 ppt

Source: Company data, Bloomberg, CMBIS

Figure 2: Revenue breakdown

RMB mn	FY18	1Q19	2Q19	3Q19	4Q19	FY19	FY20E	FY21E	FY22E
<b>Revenue</b>									
Dynamic components	8,675	1,880	1,766	2,280	2,241	8,167	7,533	7,863	8,196
MEMS components	814	154	226	289	259	929	1,014	1,064	1,118
Haptics & RF	8,073	1,530	1,496	2,118	2,457	7,694	7,627	7,675	7,685
Others (incl. optics)	569	189	327	324	347	1,094	1,887	3,718	4,731
<b>Total</b>	<b>18,131</b>	<b>3,753</b>	<b>3,815</b>	<b>5,012</b>	<b>5,305</b>	<b>17,884</b>	<b>18,060</b>	<b>20,321</b>	<b>21,729</b>
<b>Revenue mix</b>									
Dynamic components	48%	50%	46%	45%	42%	46%	42%	39%	38%
MEMS components	4%	4%	6%	6%	5%	5%	6%	5%	5%
Haptics & RF	45%	41%	39%	42%	46%	43%	42%	38%	35%
Others (incl. optics)	3%	5%	9%	6%	7%	6%	10%	18%	22%
<b>YoY Growth (%)</b>									
Dynamic components	-9%	-22%	-6%	-9%	19%	-6%	-8%	4%	4%
MEMS components	-4%	-14%	37%	8%	28%	14%	9%	5%	5%
Haptics & RF	-22%	-20%	-3%	5%	-6%	-5%	-1%	1%	0%
Others (incl. optics)	63%	36%	62%	267%	147%	92%	73%	97%	27%
<b>Total</b>	<b>-14%</b>	<b>-19%</b>	<b>1%</b>	<b>3%</b>	<b>10%</b>	<b>-1%</b>	<b>1%</b>	<b>13%</b>	<b>7%</b>
<b>Gross profit margin</b>									
Dynamic components	37.2%	32.9%	27.2%	33.3%	30.2%	31.0%	29.3%	30.5%	31.0%
MEMS components	26.6%	18.5%	26.9%	31.3%	29.3%	27.5%	29.1%	29.0%	30.0%
Haptics & RF	40.6%	32.3%	27.2%	29.5%	30.7%	29.6%	29.4%	30.4%	30.4%
Others (incl. optics)	4.0%	-6.2%	2.3%	2.6%	9.0%	3.2%	15.0%	23.0%	25.0%
<b>Total</b>	<b>37.2%</b>	<b>30.1%</b>	<b>25.0%</b>	<b>29.6%</b>	<b>29.0%</b>	<b>28.6%</b>	<b>27.9%</b>	<b>29.0%</b>	<b>29.4%</b>

Source: Company data, CMBIS

Figure 3: P&L forecast

RMB mn	1Q19	2Q19	3Q19	4Q19	FY19	1Q20E	2Q20E	3Q20E	4Q20E	FY20E
<b>Revenue</b>	3,753	3,815	5,012	5,305	<b>17,884</b>	3,102	4,009	5,023	5,927	<b>18,060</b>
...YoY	-19.1%	0.8%	2.9%	9.6%	-1.4%	-17.4%	5.1%	0.2%	11.7%	1.0%
Cost of sales	(2,623)	(2,860)	(3,528)	(3,765)	(12,777)	(2,215)	(3,008)	(3,557)	(4,250)	(13,030)
<b>Gross profit</b>	<b>1,129</b>	<b>955</b>	<b>1,483</b>	<b>1,539</b>	<b>5,107</b>	<b>887</b>	<b>1,000</b>	<b>1,466</b>	<b>1,677</b>	<b>5,030</b>
GPM (%)	30.1%	25.0%	29.6%	29.0%	28.6%	28.6%	25.0%	29.2%	28.3%	27.9%
...YoY	-36.0%	-28.3%	-17.8%	-16.5%	-24.3%	-21.5%	4.8%	-1.2%	9.0%	-1.5%
SG&A	(230)	(182)	(221)	(285)	(918)	(192)	(193)	(221)	(318)	(925)
...% of rev	-6.1%	-4.8%	-4.4%	-5.4%	-5.1%	-6.2%	-4.8%	-4.4%	-5.4%	-5.1%
R&D	(412)	(419)	(433)	(453)	(1,717)	(310)	(441)	(432)	(504)	(1,687)
...% of rev	-11.0%	-11.0%	-8.6%	-8.5%	-9.6%	-10.0%	-11.0%	-8.6%	-8.5%	-9.3%
<b>Operating</b>	<b>488</b>	<b>354</b>	<b>829</b>	<b>801</b>	<b>2,472</b>	<b>384</b>	<b>366</b>	<b>813</b>	<b>855</b>	<b>2,419</b>
OPM (%)	13.0%	9.3%	16.5%	15.1%	13.8%	12.4%	9.1%	16.2%	14.4%	13.4%
...YoY	-59.0%	-53.8%	-29.4%	-29.4%	-42.0%	-21.2%	3.5%	-1.9%	6.7%	-2.1%
<b>Net profit</b>	<b>432</b>	<b>338</b>	<b>695</b>	<b>757</b>	<b>2,222</b>	<b>339</b>	<b>338</b>	<b>679</b>	<b>805</b>	<b>2,161</b>
NPM (%)	11.5%	8.9%	13.9%	14.3%	12.4%	10.9%	8.4%	13.5%	13.6%	12.0%
...YoY	-61.6%	-48.2%	-28.6%	-27.5%	-41.5%	-21.5%	-0.1%	-2.4%	6.4%	-2.8%

Source: Company data, CMBIS

## Earnings Revision

### Our FY20/21E EPS are 31%/26% below consensus

We reduced our FY20/21E EPS by 20%/7% to reflect lower revenue/margin assumptions. Our EPS are lower than consensus by 26-31% mainly due to more conservative gross margin and revenue estimates for acoustics/haptics segment.

Figure 4: CMBI earnings revisions

(RMB mn)	New		Old		Diff (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Revenue	18,060	20,321	19,657	20,556	-8%	-1%
Gross profit	5,035	5,901	5,864	6,202	-14%	-5%
Operating profit	2,419	3,010	3,067	3,277	-21%	-8%
Net profit	2,161	2,718	2,718	2,913	-20%	-7%
EPS (RMB)	1.79	2.25	2.24	2.40	-20%	-7%
Gross margin	27.9%	29.0%	29.8%	30.1%	-2 ppt	-1.1 ppt
Operating margin	13.4%	14.8%	15.6%	15.9%	-2.2 ppt	-1.1 ppt
Net Margin	12.0%	13.4%	13.8%	14.2%	-1.9 ppt	-0.8 ppt

Source: Company data, CMBIS estimates

Figure 5: CMBI estimates vs consensus

(RMB mn)	CMBI		Consensus		Diff (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Revenue	18,060	20,321	20,506	22,841	-12%	-11%
Gross profit	5,035	5,901	6,480	7,405	-22%	-20%
Operating profit	2,419	3,010	3,640	4,200	-34%	-28%
Net profit	2,161	2,718	3,118	3,707	-31%	-27%
EPS (RMB)	1.79	2.25	2.57	3.05	-31%	-26%
Gross margin	27.9%	29.0%	31.6%	32.4%	-3.8 ppt	-3.4 ppt
Operating margin	13.4%	14.8%	17.7%	18.4%	-4.4 ppt	-3.6 ppt
Net Margin	12.0%	13.4%	15.2%	16.2%	-3.2 ppt	-2.9 ppt

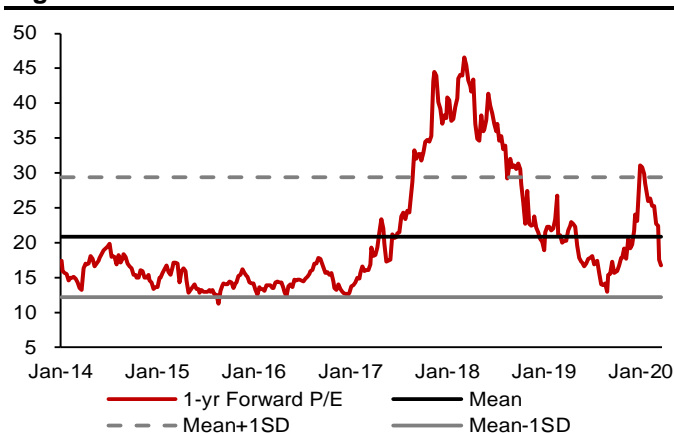
Source: Bloomberg, CMBIS estimates

## Valuation

### Maintain Sell with new TP HK\$35.8

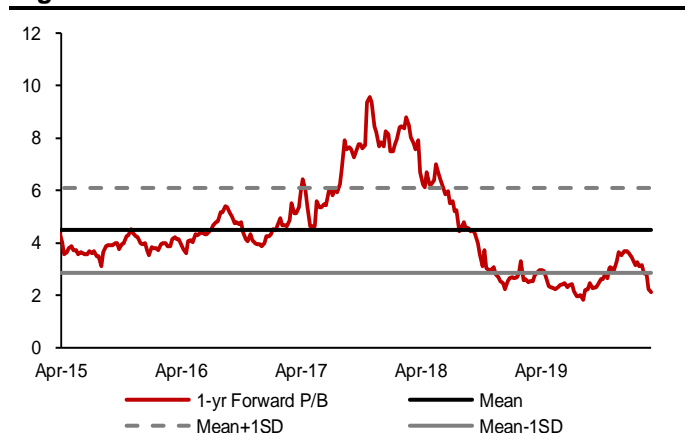
We maintain Sell for our cautious view on iPhone launch delay, optics guidance and order uncertainty. Although recent 40% correction have reflected 1H20 weakness and COVID-19 supply impact, we believe there is still downside on consensus earnings due to product launch delays and demand weakness. Our new TP of HK\$35.8 is based on same 18x FY20E P/E. Upside risks include stronger lens, better iPhone and better GPM.

Figure 6: 12M forward P/E band



Source: Company data, CMBIS

Figure 7: 12M forward P/B band



Source: Company data, CMBIS

## Financial Summary

### Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Revenue</b>	18,131	17,884	18,060	20,321	21,729
COGS	(11,388)	(12,777)	(13,030)	(14,426)	(15,335)
<b>Gross profit</b>	<b>6,743</b>	<b>5,107</b>	<b>5,030</b>	<b>5,895</b>	<b>6,395</b>
Selling and marketing	(317)	(275)	(277)	(345)	(369)
Administrative	(650)	(643)	(647)	(711)	(761)
R&D	(1,512)	(1,717)	(1,687)	(1,829)	(1,956)
<b>Operating profit</b>	<b>4,265</b>	<b>2,472</b>	<b>2,419</b>	<b>3,010</b>	<b>3,309</b>
Financial cost	(218)	(248)	(248)	(248)	(248)
Other income/(losses)	264	329	310	327	345
<b>Pre-tax profit</b>	<b>4,310</b>	<b>2,552</b>	<b>2,480</b>	<b>3,088</b>	<b>3,406</b>
Tax	(514)	(330)	(319)	(371)	(409)
Minority interest	-	-	-	-	-
<b>Net profit</b>	<b>3,796</b>	<b>2,222</b>	<b>2,161</b>	<b>2,718</b>	<b>2,997</b>

### Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Profit before taxation</b>	<b>4,310</b>	<b>2,552</b>	<b>2,480</b>	<b>3,088</b>	<b>3,406</b>
Depreciation	1,750	1,803	2,003	2,203	2,403
Change in working capital	1,149	(627)	216	(1,251)	708
Others	(420)	(85)	(69)	(97)	(145)
<b>Net cash from operating</b>	<b>6,789</b>	<b>3,644</b>	<b>4,630</b>	<b>3,944</b>	<b>6,373</b>
Capex	(2,941)	(3,000)	(2,800)	(2,800)	(2,800)
Other	(658)	68	0	0	0
<b>Net cash from investing</b>	<b>(3,599)</b>	<b>(2,932)</b>	<b>(2,800)</b>	<b>(2,800)</b>	<b>(2,800)</b>
Net borrowings	(555)	0	0	0	0
Interest paid	(216)	(248)	(248)	(248)	(248)
Dividend paid	(2,182)	(1,531)	(1,489)	(951)	(1,049)
Other	(294)	0	0	0	0
<b>Net cash from financing</b>	<b>(3,247)</b>	<b>(1,779)</b>	<b>(1,737)</b>	<b>(1,199)</b>	<b>(1,297)</b>
<b>Net change in cash</b>	<b>(57)</b>	<b>(1,068)</b>	<b>93</b>	<b>(56)</b>	<b>2,276</b>
Cash at beg of year	4,034	4,059	2,991	3,085	3,029
Exchange difference	81	0	0	0	0
<b>Cash at end of year</b>	<b>4,059</b>	<b>2,991</b>	<b>3,085</b>	<b>3,029</b>	<b>5,305</b>

### Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Current assets</b>	<b>11,985</b>	<b>11,918</b>	<b>11,129</b>	<b>13,819</b>	<b>14,681</b>
Cash & equivalents	4,126	2,991	3,085	3,029	5,305
Trade and other rev.	4,474	6,930	4,556	8,220	5,514
Inventories	3,319	1,931	3,424	2,505	3,797
Other current assets	65	65	65	65	65
<b>Non-current assets</b>	<b>17,884</b>	<b>19,080</b>	<b>19,877</b>	<b>20,474</b>	<b>20,870</b>
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
<b>Total assets</b>	<b>29,869</b>	<b>30,998</b>	<b>31,006</b>	<b>34,292</b>	<b>35,552</b>
<b>Current liabilities</b>	<b>8,317</b>	<b>8,754</b>	<b>8,090</b>	<b>9,610</b>	<b>8,921</b>
Short-term borrowings	3,493	3,493	3,493	3,493	3,493
Trade & other payables	4,548	4,989	4,322	5,816	5,111
Tax payables	205	202	204	230	246
Other current liabilities	71	71	71	71	71
<b>Non-current liabilities</b>	<b>2,618</b>	<b>2,618</b>	<b>2,618</b>	<b>2,618</b>	<b>2,618</b>
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
<b>Total liabilities</b>	<b>10,935</b>	<b>11,373</b>	<b>10,708</b>	<b>12,228</b>	<b>11,539</b>
Share capital	99	99	99	99	99
Reserves	18,835	19,527	20,199	21,965	23,914
Minority interest	-	-	-	-	-
<b>Shareholders' equity</b>	<b>18,934</b>	<b>19,626</b>	<b>20,298</b>	<b>22,064</b>	<b>24,013</b>
<b>Total equity &amp; liabilities</b>	<b>29,869</b>	<b>30,998</b>	<b>31,006</b>	<b>34,292</b>	<b>35,552</b>

### Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Sales mix (%)</b>					
Dynamic components	47.8	45.7	41.7	38.7	37.7
MEMS (microphone)	4.5	5.2	5.6	5.2	5.1
Electro. (haptics)	44.5	43.0	42.2	37.8	35.4
Other	3.1	6.1	10.4	18.3	21.8
<b>Growth (%)</b>					
Revenue	(14.1)	(1.4)	1.0	12.5	6.9
Gross profit	(22.7)	(24.3)	(1.5)	17.2	8.5
Operating Income	(29.9)	(42.0)	(2.1)	24.4	9.9
Net profit	(28.7)	(41.5)	(2.8)	25.8	10.3
<b>Profitability (%)</b>					
Gross Margin	37.2	28.6	27.9	29.0	29.4
Operating Margin	23.5	13.8	13.4	14.8	15.2
Net margin	20.9	12.4	12.0	13.4	13.8
<b>Balance sheet ratios</b>					
Net debt/total equity (x)	0.1	0.1	0.1	0.1	0.0
Current ratio (x)	1.4	1.4	1.4	1.4	1.6
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
<b>Returns (%)</b>					
ROE	20.0	11.3	10.6	12.3	12.5
ROA	12.7	7.2	7.0	7.9	8.4
<b>Per share data (RMB)</b>					
EPS	3.12	1.84	1.79	2.25	2.48
DPS	1.79	1.27	1.23	0.79	0.87

Source: Company data, CMBIS estimates

# Disclosures & Disclaimers

## Analyst Certification

The research analyst who is primary responsible for the content of this research report, in whole or in part, certifies that with respect to the securities or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by that analyst in this report.

Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the stock(s) covered in this research report 3 business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong listed companies covered in this report; and (4) have any financial interests in the Hong Kong listed companies covered in this report.

## CMBIS Ratings

**BUY** : Stock with potential return of over 15% over next 12 months  
**HOLD** : Stock with potential return of +15% to -10% over next 12 months  
**SELL** : Stock with potential loss of over 10% over next 12 months  
**NOT RATED** : Stock is not rated by CMBIS

**OUTPERFORM** : Industry expected to outperform the relevant broad market benchmark over next 12 months  
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