

# Weichai Power-A (000338 CH)

## Expect further earnings cut by the Street; Prefer Weichai-H for large valuation discount

Weichai's net profit in 3Q22 came in at RMB925mn, down 37% YoY (before restatement), which is below expectations. Weichai's 3Q results were hit by both the core business (engine + HDT) and the European business (KION Group, KGX GR). We slash our earnings forecast in 2022E/23E/24E by 47%/40%/37% (34%/35%/31% below consensus). We expect the Street to further revise down the earnings forecast. Our SOTP-based TP is revised down to RMB9.3. We maintain **HOLD** on Weichai-A but prefer Weichai-H for more attractive valuation (the current H/A discount is 23%, vs historical average of 12%). We see potential earnings recovery in 2023E, driven by both the recovery of HDT (sensitive to GDP growth) and agricultural machinery engine (import substitution).

- **3Q22 results highlights.** Revenue increased 9% YoY to RMB43.8bn in 3Q22. The increase in revenue was driven by the consolidation of LOVOL Heavy (agricultural machinery business). Revenue slightly dropped 2% for like-for-like comparison. Gross margin narrowed 5.1ppt YoY and 1.6ppt QoQ to 15.3%. EBIT was RMB549mn (-75% YoY), largely contributed by other income and gains that offset the weak margin. Net profit dropped 37% YoY to RMB925mn, helped by tax credit and positive MI (adjustment of net loss of KION and other business). In 9M22, revenue /net profit dropped 22%/58% to RMB130bn/3.3bn. Operating cash flow in 9M22 deteriorated to -RMB2.4bn (9M21: Inflow of RMB3.67bn).
- **Engine sales stabilizing.** According to CICEIA, Weichai's multi-cylinder sales dropped 18% YoY to 137k units in 3Q22, with a market share of ~15%. The monthly sales volume stabilized at 44-46k units in 3Q. In 9M22, sales volume declined ~49% YoY to 414k units.
- **Take time to see recovery of KION's business.** KION Group (45.2% owned by Weichai) reported a net loss of EUR93mn in 3Q22 (net profit of EUR140mn in 3Q21). Supply Chain Solutions (SCS) segment, a major source of the loss, was hit by project delays as a result of supply chain disruptions. Industrial Trucks & Services (ITS) segment was also hit by increased cost of materials, energy and logistics. KION guided that the full year adjusted EBIT to be EUR200-310mn, which implies a wide range of -EUR10mn to +EUR100mn in 4Q22E. It's worth noting that KION's net debt increased 2.3x YoY to EUR1.86bn as at end-Sep 2022.

### Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (RMB mn)	197,491	203,548	166,269	183,926	197,040
YoY growth (%)	13.3	3.1	(18.3)	10.6	7.1
Net income (RMB mn)	9,207	9,255	4,229	5,535	6,453
EPS (RMB)	1.16	1.06	0.48	0.63	0.74
YoY growth (%)	1.1	(8.6)	(54.3)	30.9	16.6
Consensus EPS (RMB)	n/a	n/a	0.73	0.98	1.07
P/E (x)	7.3	8.2	19.0	14.5	12.4
EV / EBITDA (x)	3.2	2.9	4.4	3.5	3.2
P/B (x)	1.3	1.1	1.1	1.1	1.0
Yield (%)	4.8	4.2	1.8	2.4	2.8
ROE (%)	19.1	15.2	5.9	7.5	8.2
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIGM estimates

### HOLD (Maintain)

Target Price	RMB9.30
(Previous TP	RMB13.20)
Up/Downside	+1%
Current Price	RMB9.20

### China Capital Goods

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### Stock Data

Mkt Cap (RMB mn)	76,233
Avg 3 mths t/o (RMB mn)	345
52w High/Low (RMB)	19.09/9.10
Total Issued Shares (mn)	1,934 (H)
	6,783 (A)

Source: Bloomberg

### Shareholding Structure

Weichai Holdings Group	16.3%
Weifang Investment Group	3.4%
CCASS	4.2%
Free float (H-share)	22.2%
Free float (A-share)	53.9%

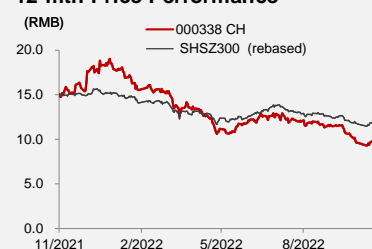
Source: HKEx, Company data

### Share Performance

	Absolute	Relative
1-mth	-4.2%	3.6%
3-mth	-23.1%	-9.5%
6-mth	-17.8%	-6.8%

Source: Bloomberg

### 12-mth Price Performance



Source: Bloomberg

### Auditor: Ernst & Young

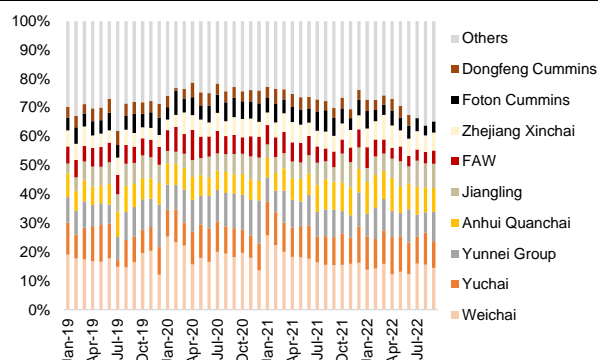
### Related Reports

1. Weichai Power (000338 CH, HOLD) – Short-term earnings under pressure; Import substitution strategy to support long-term earnings – 4 Apr 2022 ([link](#))
2. China HDT Sector - Lower industry forecast on weak recovery; D/G Weichai-A; BUY Weichai & Sinotruk on valuation – 25 Mar 2022 ([link](#))

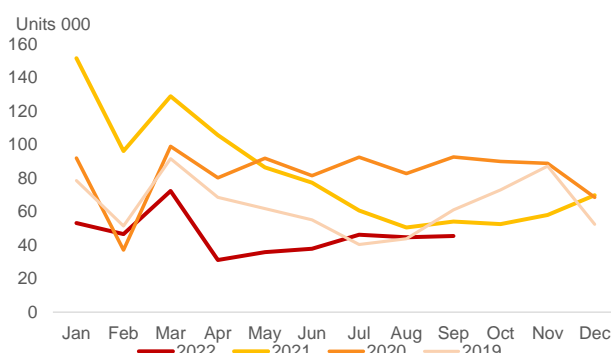
**Figure 1: Weichai's quarterly results**

(RMB mn)	1Q21	1Q22	Chg (YoY)	2Q21	2Q22	Chg (YoY)	3Q21	3Q22	Chg (YoY)
<b>Revenue</b>	<b>65,471</b>	<b>41,104</b>	<b>-37%</b>	<b>60,917</b>	<b>45,636</b>	<b>-25%</b>	<b>40,041</b>	<b>43,783</b>	<b>9%</b>
Cost of sales	(52,929)	(33,445)	-37%	(49,648)	(37,924)	-24%	(31,888)	(37,080)	16%
<b>Gross profit</b>	<b>12,542</b>	<b>7,659</b>	<b>-39%</b>	<b>11,269</b>	<b>7,712</b>	<b>-32%</b>	<b>8,153</b>	<b>6,704</b>	<b>-18%</b>
Other income	159	168	6%	243	202	-17%	133	254	92%
Other gains and losses	214	139	-35%	106	505	376%	170	599	252%
S&D expenses	(3,408)	(2,553)	-25%	(2,905)	(2,459)	-15%	(2,630)	(2,799)	6%
Administrative expenses	(2,227)	(1,878)	-16%	(1,983)	(2,000)	1%	(1,897)	(2,007)	6%
R&D expenses	(1,728)	(1,828)	6%	(1,839)	(1,860)	1%	(1,471)	(1,827)	24%
Taxes and surcharges	(270)	(82)	-70%	(245)	(139)	-43%	(78)	(100)	27%
Impairment loss of assets	(237)	(220)	-7%	(21)	(420)	1888%	(152)	(277)	83%
<b>EBIT</b>	<b>5,046</b>	<b>1,405</b>	<b>-72%</b>	<b>4,624</b>	<b>1,539</b>	<b>-67%</b>	<b>2,228</b>	<b>549</b>	<b>-75%</b>
Other expenses	(28)	(39)	38%	(24)	(20)	-16%	(12)	(24)	103%
Net finance cost	98	156	58%	97	371	281%	194	67	-66%
Share of profit of JV and associates	63	58	-8%	95	(51)	n/a	43	(59)	n/a
<b>Pretax profit</b>	<b>5,179</b>	<b>1,579</b>	<b>-70%</b>	<b>4,793</b>	<b>1,839</b>	<b>-62%</b>	<b>2,453</b>	<b>533</b>	<b>-78%</b>
Income tax	(812)	(270)	-67%	(905)	(196)	-78%	(517)	252	n/a
<b>After tax profit</b>	<b>4,367</b>	<b>1,309</b>	<b>-70%</b>	<b>3,888</b>	<b>1,643</b>	<b>-58%</b>	<b>1,936</b>	<b>784</b>	<b>-59%</b>
MI	(1,024)	(258)	-75%	(800)	(307)	-62%	(467)	141	n/a
<b>Net profit</b>	<b>3,344</b>	<b>1,051</b>	<b>-69%</b>	<b>3,088</b>	<b>1,335</b>	<b>-57%</b>	<b>1,469</b>	<b>925</b>	<b>-37%</b>
<b>Key ratios</b>			<b>Chg (ppt)</b>			<b>Chg (ppt)</b>			<b>Chg (ppt)</b>
Gross margin	19.2%	18.6%	-0.5	18.5%	16.9%	-1.6	20.4%	15.3%	-5.1
S&D expense ratio	5.2%	6.2%	1.0	4.8%	5.4%	0.6	6.6%	6.4%	-0.2
Administrative expense ratio	3.4%	4.6%	1.2	3.3%	4.4%	1.1	4.7%	4.6%	-0.2
R&D expense ratio	2.6%	4.4%	1.8	3.0%	4.1%	1.1	3.7%	4.2%	0.5
Effective tax rate	15.7%	17.1%	1.4	18.9%	10.7%	-8.2	21.1%	-47.3%	-68.4

Source: Company data, CMBIGM

**Figure 2: China multi-cylinder engine market share**

Source: CICEIA, CMBIGM

**Figure 3: Weichai's multi-cylinder engine monthly sales volume**

Source: CICEIA, CMBIGM

**Figure 4: KION's latest guidance for 2022E**

KION (EUR mn)	2020	2021	2022E guidance	
			Low-end	High-end
<b>Order intake</b>	<b>9,443</b>	<b>12,482</b>	<b>11,600</b>	<b>12,500</b>
Growth (YoY)	4%	32%	-7%	0%
<b>Revenue</b>	<b>8,342</b>	<b>10,294</b>	<b>10,450</b>	<b>11,250</b>
Growth (YoY)	-5%	23%	2%	9%
<b>Adjusted EBIT</b>	<b>547</b>	<b>842</b>	<b>200</b>	<b>310</b>
Growth (YoY)	-36%	54%	-76%	-63%
<b>Adjusted EBIT margin</b>	<b>6.6%</b>	<b>8.2%</b>	<b>1.9%</b>	<b>2.8%</b>
<b>Net income</b>	<b>211</b>	<b>568</b>	-	-
Growth (YoY)	-53%	169%	-	-

Source: Company data, CMBIGM

**Figure 5: KION's quarterly financials**

KION (EUR mn)	1Q22	2Q22	3Q22
<b>Order intake</b>	<b>2,900</b>	<b>3,755</b>	<b>2,517</b>
Growth (YoY)	10%	15%	-19%
<b>Revenue</b>	<b>2,734</b>	<b>2,802</b>	<b>2,706</b>
Growth (YoY)	15%	8%	5%
<b>Adjusted EBIT</b>	<b>170</b>	<b>141</b>	<b>-101</b>
Growth (YoY)	-21%	-43%	n/a
<b>Adjusted EBIT margin</b>	<b>6.2%</b>	<b>5.0%</b>	<b>-3.7%</b>
<b>Net income</b>	<b>80</b>	<b>80</b>	<b>-93</b>
Growth (YoY)	-41%	-48%	n/a

Source: Company data, CMBIGM

Figure 6: Change in key assumptions for Weichai

Change in key assumptions	2022E			2023E			2024E		
Sales volume (unit)	Old	New	Change	Old	New	Change		New	Change
Engine total	942,824	699,288	-25.8%	1,009,983	809,552	-19.8%	1,077,942	889,728	-17.5%
HDT (Shaanxi Heavy-duty Motor)	112,500	67,500	-40.0%	118,125	72,900	-38.3%	118,125	74,358	-37.1%
Gear box (Shaanxi Fast Gear Company)	1,072,290	576,500	-46.2%	1,093,736	605,325	-44.7%	1,093,736	617,432	-43.5%
(RMB mn)									
Revenue									
Diesel engines	56,569	41,957	-25.8%	61,609	49,383	-19.8%	66,832	55,163	-17.5%
Automobiles and major components	63,979	34,776	-45.6%	66,652	37,302	-44.0%	66,652	38,048	-42.9%
Forklift trucks & supply chain solution	79,018	79,018	0.0%	83,759	85,339	1.9%	88,784	90,459	1.9%
Agricultural machinery	-	18,306	-	-	20,503	-	-	22,553	-
Intersegment sales	(14,967)	(7,788)	-48.0%	(15,902)	(8,601)	-45.9%	(16,670)	(9,184)	-44.9%
Total revenue	184,598	166,269	-9.9%	196,119	183,926	-6.2%	205,599	197,040	-4.2%
Segment profit									
Diesel engines	5,940	2,727	-54.1%	6,777	3,704	-45.3%	7,352	4,413	-40.0%
Automobiles and major components	(320)	(1,009)	n/a	333	149	-55.2%	733	304	-58.5%
Forklift trucks & supply chain solution	5,373	1,027	-80.9%	5,696	1,536	-73.0%	6,126	1,809	-70.5%
Agricultural machinery	-	769	-	-	902	-	-	1,015	-
Intersegment sales	(150)	(78)	-48.0%	(159)	(86)	-45.9%	(167)	(92)	-44.9%
Total segment profit	10,843	3,437	-68.3%	12,647	6,205	-50.9%	14,044	7,450	-47.0%
Segment margin			Chg (ppt)			Chg (ppt)			Chg (ppt)
Diesel engines	10.5%	6.5%	-4.0	11.0%	7.5%	-3.5	11.0%	8.0%	-3.0
Automobiles and major components	-0.5%	-2.9%	-2.4	0.5%	0.4%	-0.1	1.1%	0.8%	-0.3
Forklift trucks & supply chain solution	6.8%	1.3%	-5.5	6.8%	1.8%	-5.0	6.9%	2.0%	-4.9
Agricultural machinery	-	4.2%	-	-	4.4%	-	-	4.5%	-
Average	5.9%	2.1%	-3.8	6.4%	3.4%	-3.1	6.8%	3.8%	-3.1
Net profit	7,936	4,229	-46.7%	9,191	5,535	-39.8%	10,283	6,453	-37.3%

Source: Company data, CMBIGM estimates

Figure 7: SOTP valuation

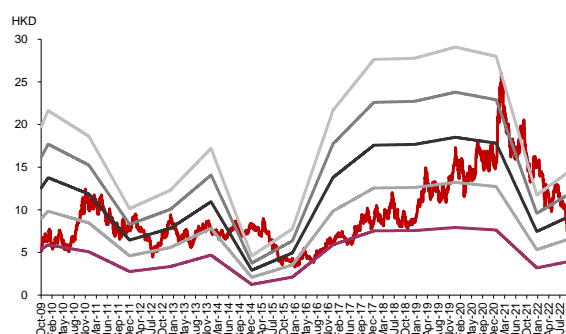
SOTP valuation	Valuation methodology	Target multiple (x)	EBITDA 2022E (RMB mn)	Estimated EV (RMB mn)	Net cash / (Net debt)	Equity value (RMB mn)	Equity value breakdown
Weichai core business	EV/EBITDA	5.5	5,099	28,043	42,049	70,092	86.4%
KION Group	Proportionate market value	-	-	-	-	9,516	11.7%
Ballard Power Systems	Proportionate market value	-	-	-	-	2,391	2.9%
Ceres Power	Proportionate market value	-	-	-	-	1,043	1.3%
Share of JV/associates	P/B	1.0	-	-	-	3,518	4.3%
Minority interest in core business						(5,421)	-6.7%
Total NAV						81,140	100.0%
NAV per share (RMB)						9.3	
NAV per share (HK\$)						10.1	

Note 1: Weichai owns 45.2% interest in KION, 20% interest in Ballard Power and 20% interest in Ceres Power.

Note 2: Share of JV / associates exclude Ballard Power and Ceres Power

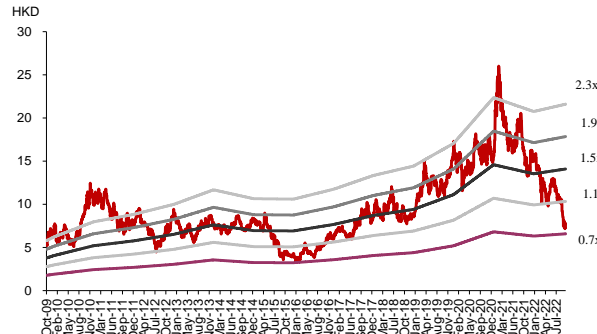
Source: Company data, CMBIGM estimates

Figure 8: Weichai Power-H P/E band

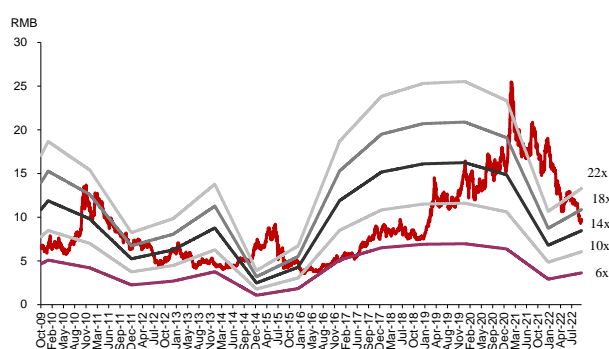


Source: Bloomberg, Company data, CMBIGM estimates

Figure 9: Weichai Power-H P/B band



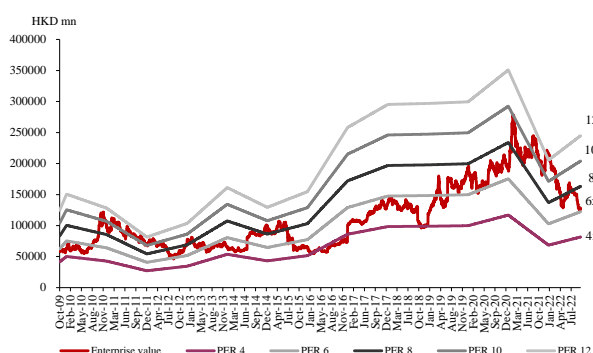
Source: Bloomberg, Company data, CMBIGM estimates

**Figure 10: Weichai Power-A P/E band**

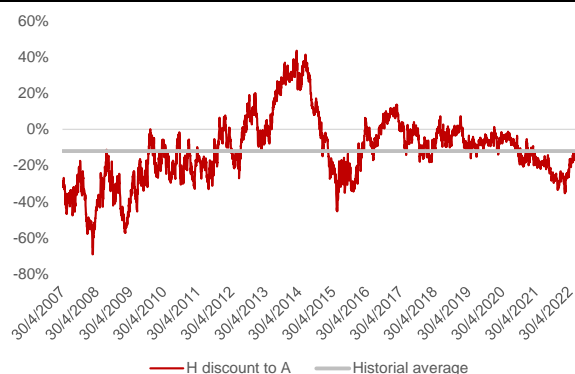
Source: Bloomberg, Company data, CMBIGM estimates

**Figure 11: Weichai Power-A P/B band**

Source: Bloomberg, Company data, CMBIGM estimates

**Figure 12: Weichai Power EV/EBITDA band**

Source: Bloomberg, Company data, CMBIGM estimates

**Figure 13: Weichai Power H discount to A**

Source: Bloomberg, CMBIGM

**Upside risks:** (1) Recovery of China economy; (2) Improvement of supply chain in Europe. **Downside risks:** (1) Further weakness in engine demand; (2) Increase in component cost; (3) New business growth below expectations.

## Financial Summary

### Income statement

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Revenue</b>	<b>197,491</b>	<b>203,548</b>	<b>166,269</b>	<b>183,926</b>	<b>197,040</b>
Cost of sales	(159,353)	(163,947)	(138,004)	(148,244)	(158,618)
<b>Gross profit</b>	<b>38,138</b>	<b>39,601</b>	<b>28,266</b>	<b>35,682</b>	<b>38,423</b>
Operating expenses	(25,289)	(26,038)	(23,745)	(28,416)	(29,917)
<b>EBIT</b>	<b>12,850</b>	<b>13,563</b>	<b>4,521</b>	<b>7,265</b>	<b>8,506</b>
Other expenses	(142)	(145)	(200)	(221)	(236)
Net finance cost	(279)	450	686	347	484
Finance income and others	1,278	1,724	1,898	1,576	1,730
Finance expenses	(1,557)	(1,274)	(1,212)	(1,230)	(1,246)
profit of JV & associates	253	187	216	240	244
<b>Pretax profit</b>	<b>12,682</b>	<b>14,055</b>	<b>5,224</b>	<b>7,631</b>	<b>8,997</b>
Income tax	(1,407)	(2,493)	(627)	(1,412)	(1,664)
<b>After tax profit</b>	<b>11,275</b>	<b>11,562</b>	<b>4,597</b>	<b>6,219</b>	<b>7,333</b>
MI	(2,068)	(2,307)	(368)	(684)	(880)
<b>Net profit</b>	<b>9,207</b>	<b>9,255</b>	<b>4,229</b>	<b>5,535</b>	<b>6,453</b>
D&A	8,858	10,597	11,053	12,210	12,867
<b>EBITDA</b>	<b>21,708</b>	<b>24,160</b>	<b>15,574</b>	<b>19,475</b>	<b>21,373</b>

### Cash flow summary

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Pretax profit	12,682	14,055	5,224	7,631	8,997
Finance cost	1,557	1,274	1,212	1,230	1,246
Interest income	(1,278)	(1,724)	(1,898)	(1,576)	(1,730)
Share of profit or loss of associates	(253)	(187)	(216)	(240)	(244)
Depreciation	6,699	8,473	8,949	9,999	10,549
Amortization of intangible assets	2,087	2,065	2,042	2,150	2,257
Income tax paid	(1,407)	(2,493)	(627)	(1,412)	(1,664)
Change in working capital	1,114	(8,767)	(11,392)	(3,022)	(4,167)
Others	1,727	1,963	1,960	1,638	1,792
<b>Cash flow from operation</b>	<b>22,928</b>	<b>14,658</b>	<b>5,254</b>	<b>16,398</b>	<b>17,035</b>
Net capex on PP&E	(5,992)	(3,610)	(10,700)	(8,700)	(6,700)
Investment in JV/associates	(537)	(3,082)	0	0	0
Investment in subsidiaries	(938)	(496)	0	0	0
Dividend received	145	143	123	137	139
Others	(2,095)	1,636	0	0	0
<b>Cash flow from investing</b>	<b>(9,417)</b>	<b>(5,409)</b>	<b>(10,577)</b>	<b>(8,563)</b>	<b>(6,561)</b>
Proceeds from equity financing	0	14,050	0	0	0
Net bank borrowings	1,052	(5,913)	300	800	100
Dividend paid	(3,459)	(4,837)	(3,229)	(1,480)	(1,937)
Interest paid	0	0	(1,212)	(1,230)	(1,246)
Others	(579)	(176)	0	0	0
<b>Cash flow from financing</b>	<b>(2,986)</b>	<b>3,123</b>	<b>(4,141)</b>	<b>(1,910)</b>	<b>(3,083)</b>
Change in cash	10,525	12,372	(9,463)	5,924	7,391
Cash at beginning of the year	48,818	62,216	75,043	65,580	71,504
Exchange gains/(losses) and others	2,873	455	0	0	0
Cash at the end of the year	62,216	75,043	65,580	71,504	78,896

### Balance sheet

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Non-current assets</b>	<b>118,235</b>	<b>116,406</b>	<b>116,208</b>	<b>112,863</b>	<b>106,862</b>
PP&E	31,720	33,188	33,239	30,240	24,692
Investment in JV/associates	4,944	6,713	6,806	6,909	7,014
Goodwill	24,666	22,847	22,847	22,847	22,847
Long term receivables	9,623	9,522	9,522	9,522	9,522
Intangible assets	23,826	20,908	20,566	20,116	19,560
Others	23,457	23,228	23,228	23,228	23,228
<b>Current assets</b>	<b>152,515</b>	<b>160,638</b>	<b>155,149</b>	<b>176,719</b>	<b>180,929</b>
Prepayments	1,095	1,570	1,508	1,446	1,384
Inventories	31,226	31,585	36,471	41,509	43,666
Trade receivables	15,422	18,191	17,341	28,011	22,734
Notes receivables	28,780	16,562	16,562	16,562	16,562
Others	13,775	17,688	17,688	17,688	17,688
Cash	62,216	75,043	65,580	71,504	78,896
<b>Current liabilities</b>	<b>123,713</b>	<b>115,382</b>	<b>108,827</b>	<b>122,313</b>	<b>115,127</b>
Trade and bills payables	45,450	39,596	32,241	44,927	37,641
Notes payable	22,970	27,797	27,797	27,797	27,797
Bank borrowings	17,006	12,982	13,782	14,582	14,682
Others	38,287	35,006	35,006	35,006	35,006
<b>Non-current liabilities</b>	<b>66,604</b>	<b>58,700</b>	<b>58,200</b>	<b>58,200</b>	<b>58,200</b>
Bank borrowings	20,729	18,839	18,339	18,339	18,339
Long term payables	21,205	18,427	18,427	18,427	18,427
Others	24,670	21,435	21,435	21,435	21,435
<b>Equity</b>	<b>80,433</b>	<b>102,962</b>	<b>104,330</b>	<b>109,069</b>	<b>114,464</b>
Shareholders' equity	51,202	70,907	71,907	75,962	80,478
MI	29,231	32,055	32,423	33,107	33,987

### Key ratios

YE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Sales mix (%)</b>					
Diesel engines	31.8	31.7	25.2	26.8	28.0
Automobiles and major components	43.5	36.5	20.9	20.3	19.3
Forklift trucks & supply chain solution	33.0	38.6	47.5	46.4	45.9
Agricultural machinery	-	-	11.0	11.1	11.4
Intersegment sales	(8.2)	(6.8)	(4.7)	(4.7)	(4.7)
Total	100.0	100.0	100.0	100.0	100.0
<b>Profit &amp; loss ratio (%)</b>					
Gross margin	19.3	19.5	17.0	19.4	19.5
EBIT margin	6.5	6.7	2.7	4.0	4.3
After tax profit margin	5.7	5.7	2.8	3.4	3.7
<b>Growth (%)</b>					
Revenue	13.3	3.1	(18.3)	10.6	7.1
Gross profit	0.3	3.8	(28.6)	26.2	7.7
EBIT	(10.9)	5.5	(66.7)	60.7	17.1
Net profit	1.1	0.5	(54.3)	30.9	16.6
<b>Balance sheet ratio</b>					
Current ratio (x)	1.2	1.4	1.4	1.4	1.6
Receivable turnover days	27	30	39	45	47
Inventory turnover days	64	70	90	96	98
Payable turnover days	94	95	95	95	95
Net debt / total equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash
<b>Profitability (%)</b>					
ROA	4.4	4.2	1.7	2.2	2.5
ROE	19.1	15.2	5.9	7.5	8.2
<b>Per share data</b>					
EPS (RMB)	1.16	1.06	0.48	0.63	0.74
BVPS (RMB)	6.45	8.13	8.24	8.70	9.22
DPS (RMB)	0.41	0.37	0.17	0.22	0.26

Source: Company data, CMBIGM estimates



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