26 Jan 2024

CMB International Global Markets | Equity Research | Company Update

InnoLight (300308 CH)

True beneficiary in AI value chain

We think 2024 is set to be another solid year for both infrastructure investments and downstream demand continue to thrive. According to Bloomberg's consensus, CSP3 (comprising Amazon, Google, and Microsoft) along with Meta, are projected to ramp up their capex by 16.6%/7.6% YoY in 2024/2025E. We reaffirm our positive stance on optical transceiver players, specifically in light of their ongoing capacity expansion and production ramp-up of the high data rate optical modules, e.g., 400G/800G products. **We maintain BUY on Innolight, with new TP of RMB136.**

Last week, TFC pre-announced its FY23 earnings, with NP growth of 68-88% YoY to RMB677-758mn. The robust performance was primarily driven by the lofty demand for AI computing power in data centers, boosting sales of TFC's high speed optical modules. TFC's performance underscored our confidence in Innolight, one of our top picks as a true beneficiary in AI value chain.

Considering greater-than-expected ramp-up of TSMC's CoWoS capacity and continued strong investments in AI infrastructure, we expect Innolight's 2024/25E revenue to come in better than our previous estimates. **We revised up revenue forecasts by 22%/31% and lifted GPM to 34% and 33% for 2023E/24E/25E (vs. prior 32%/32%). The new TP is based on 30x 2024E P/E,** which is close to 5-year historical average of forward P/E (vs. previously 35x, factoring in market sentiment).

We recommend investors pay special attention to the forthcoming earnings of CSP3 & Meta next week. The focus should be on their future projections for cloud revenue and capex guidelines, as these factors will be pivotal in understanding the industry's future direction.

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	7,695	9,642	11,127	18,074	20,524
YoY growth (%)	9.2	25.3	15.4	62.4	13.6
Gross margin (%)	25.6	29.3	32.6	34.0	33.0
Operating profit (RMB mn)	963	1,327	2,302	4,087	4,471
YoY growth (%)	(2.7)	37.9	73.4	77.5	9.4
Net profit (RMB mn)	877.0	1,224.0	2,035.4	3,644.7	3,978.2
YoY growth (%)	1.3	39.6	66.3	79.1	9.2
P/S (x)	12.1	9.7	8.4	5.2	4.5
P/E (x)	32.6	20.6	45.7	25.5	23.4
ROE (%)	9.1	10.4	15.5	22.7	20.4

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	**RMB136.00**
(Previous TP	RMB109.30)
Up/Downside	**17.3%**
Current Price	**RMB115.96**

China Semi

Lily YANG, Ph.D
(852) 3916 3716
lilyyang@cmbi.com.hk

Kevin ZHANG
(852) 3761 8727
kevinzhang@cmbi.com.hk

Stock Data

Mkt Cap (RMB mn)	93,092.7
Avg 3 mths t/o (RMB mn)	2,730.1
52w High/Low (RMB)	170.00/28.91
Total Issued Shares (mn)	802.8

Source: FactSet

Shareholding Structure

Shandong Zhongji Investment Holdings Co.	11.3%
Wang Weixiu	6.2%

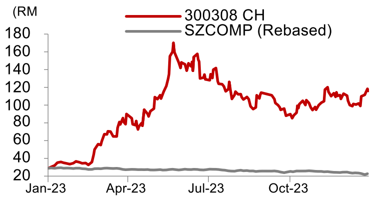
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	8.4%	14.1%
3-mth	29.0%	40.3%
6-mth	-10.1%	9.1%

Source: FactSet

12-mth Price Performance



Source: FactSet

Figure 1: CMBIGM estimates vs. consensus

RMB mn	CMBI estimates			Consensus			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	11,127	18,074	20,524	11,566	23,216	28,240	-4%	-22%	-27%
Gross Profit	3,631	6,144	6,782	3,667	7,463	9,041	-1%	-18%	-25%
Net profit	2,035	3,645	3,978	1,979	4,034	4,972	3%	-10%	-20%
EPS (RMB)	2.54	4.54	4.96	2.46	4.95	6.11	3%	-8%	-19%
Gross Margin	32.6%	34.0%	33.0%	31.7%	32.1%	32.0%	0.9 ppt	1.8 ppt	1 ppt
Net Margin	18.3%	20.2%	19.4%	17.1%	17.4%	17.6%	1.2 ppt	2.8 ppt	1.8 ppt

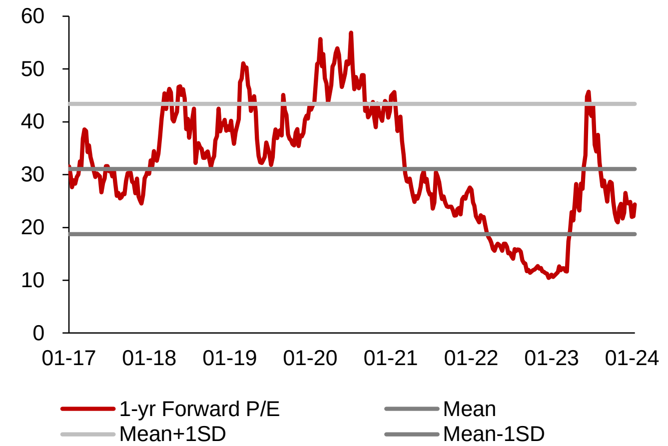
Source: Company data, CMBIGM estimates

Figure 2: CMBIGM estimates vs. consensus

RMB mn	New			Old			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	11,127	18,074	20,524	11,386	14,819	15,690	-2%	22%	31%
Gross Profit	3,631	6,144	6,782	3,656	4,707	4,980	-1%	31%	36%
Net profit	2,035	3,645	3,978	1,708	2,321	2,501	19%	57%	59%
EPS (RMB)	2.54	4.54	4.96	2.13	2.90	3.12	19%	57%	59%
Gross Margin	32.6%	34.0%	33.0%	32.1%	31.8%	31.7%	0.5 ppt	2.2 ppt	1.3 ppt
Net Margin	18.3%	20.2%	19.4%	15.0%	15.7%	15.9%	3.3 ppt	4.5 ppt	3.4 ppt

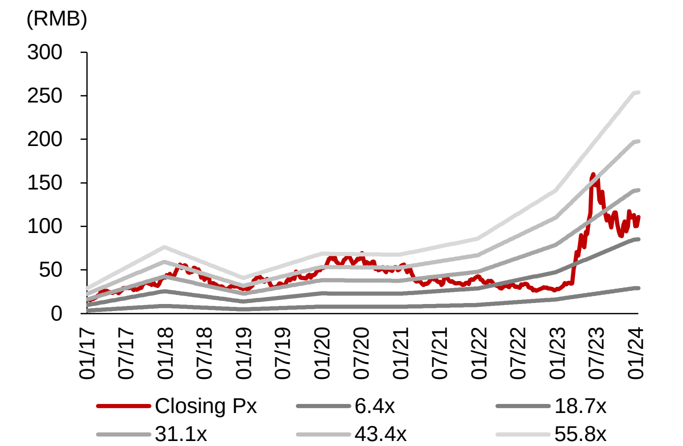
Source: Company data, CMBIGM estimates

Figure 3: 1-yr forward PE



Source: Bloomberg, CMBIGM

Figure 4: PE band



Source: Bloomberg, CMBIGM

Financial Summary

INCOME STATEMENT	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Revenue	**7,050**	**7,695**	**9,642**	**11,127**	**18,074**	**20,524**
Cost of goods sold	(5,257)	(5,727)	(6,816)	(7,496)	(11,930)	(13,742)
Gross profit	**1,793**	**1,968**	**2,826**	**3,631**	**6,144**	**6,782**
Operating expenses	**(803)**	**(1,005)**	**(1,499)**	**(1,328)**	**(2,057)**	**(2,310)**
Selling expense	(22)	(21)	(63)	(25)	(80)	(69)
SG&A expense	(477)	(507)	(598)	(575)	(918)	(1,052)
R&D expense	(506)	(541)	(767)	(676)	(1,080)	(1,206)
Others	202	64	(71)	(51)	21	16
Operating profit	**990**	**963**	**1,327**	**2,302**	**4,087**	**4,471**
Other income	0	1	28	2	28	17
Other expense	(3)	(4)	(4)	2	(2)	0
Pre-tax profit	**987**	**960**	**1,352**	**2,306**	**4,113**	**4,489**
Income tax	(111)	(73)	(118)	(242)	(431)	(471)
After tax profit	**876**	**886**	**1,234**	**2,064**	**3,681**	**4,018**
Minority interest	11	10	10	29	37	40
Net profit	**865**	**877**	**1,224**	**2,035**	**3,645**	**3,978**

BALANCE SHEET	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Current assets	**7,982**	**10,022**	**9,587**	**12,139**	**15,981**	**18,823**
Cash & equivalents	1,679	3,515	2,831	5,119	6,981	9,092
Account receivables	1,514	1,997	1,509	2,149	2,803	2,820
Inventories	3,774	3,799	3,888	3,711	4,787	5,378
Prepayment	40	72	64	111	181	205
Other current assets	973	638	1,295	1,049	1,229	1,328
Non-current assets	**5,634**	**6,543**	**6,970**	**7,530**	**8,546**	**9,656**
PP&E	2,726	3,152	3,217	3,564	4,274	5,133
Right-of-use assets	0	21	11	5	7	8
Deferred income tax	38	46	48	108	134	156
Intangibles	360	382	322	263	209	158
Goodwill	1,915	1,980	1,949	1,917	1,886	1,854
Other non-current assets	595	962	1,422	1,673	2,037	2,347
Total assets	**13,616**	**16,565**	**16,557**	**19,669**	**24,527**	**28,480**
Current liabilities	**3,772**	**3,166**	**3,264**	**3,326**	**4,017**	**4,421**
Short-term borrowings	1,041	794	385	58	141	157
Account payables	1,367	1,205	1,136	1,739	2,183	2,335
Tax payable	35	68	93	145	180	209
Other current liabilities	1,128	932	1,349	1,283	1,384	1,571
Contract liabilities	22	1	22	6	9	10
Accrued expenses	179	166	279	96	120	139
Non-current liabilities	**1,850**	**1,796**	**1,224**	**1,857**	**2,556**	**2,505**
Long-term borrowings	1,430	1,262	696	1,390	1,973	1,828
Bond payables	29	0	0	0	0	0
Deferred income	154	277	264	158	198	229
Other non-current liabilities	238	258	264	309	385	447
Total liabilities	**5,622**	**4,962**	**4,488**	**5,184**	**6,573**	**6,926**
Share capital	713	800	801	803	803	803
Retained earnings	2,090	2,861	3,893	5,743	9,075	12,529
Other reserves	5,086	7,828	7,251	7,787	7,887	7,992
Total shareholders equity	**7,889**	**11,489**	**11,945**	**14,333**	**17,765**	**21,324**
Minority interest	104	114	124	152	189	229
Total equity and liabilities	**13,616**	**16,565**	**16,557**	**19,669**	**24,527**	**28,480**

CASH FLOW	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	**987**	**960**	**1,352**	**2,306**	**4,113**	**4,489**
Depreciation & amortization	340	436	493	489	546	669
Tax paid	(111)	(73)	(118)	(242)	(431)	(471)
Change in working capital	(1,096)	(587)	291	563	(1,336)	(404)
Others	(99)	77	432	(321)	65	163
Net cash from operations	**22**	**813**	**2,449**	**2,795**	**2,957**	**4,447**
Investing						
Capital expenditure	(956)	(840)	(792)	(1,044)	(1,697)	(1,926)
Acquisition of subsidiaries/ investments	(3,728)	(1,529)	(5,967)	0	0	0
Net proceeds from disposal of short-term investments	3,959	1,109	5,167	577	0	0
Others	(147)	42	40	102	94	103
Net cash from investing	**(873)**	**(1,219)**	**(1,553)**	**(365)**	**(1,603)**	**(1,823)**
Financing						
Dividend paid	(121)	(168)	(233)	(239)	(347)	(566)
Net borrowings	1,421	(259)	(699)	(521)	667	(130)
Proceeds from share issues	0	2,665	33	461	0	0
Others	0	26	(742)	102	120	120
Net cash from financing	**1,300**	**2,264**	**(1,641)**	**(198)**	**440**	**(575)**
Net change in cash						
Cash at the beginning of the year	1,236	1,648	3,489	2,809	5,105	6,963
Exchange difference	(37)	(17)	64	64	64	64
Others	449	1,859	(745)	2,232	1,794	2,049
Cash at the end of the year	**1,648**	**3,489**	**2,809**	**5,105**	**6,963**	**9,076**

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

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.

CMBIGM 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 CMBIGM
OUTPERFORM	: Industry expected to outperform the relevant broad market benchmark over next 12 months
MARKET-PERFORM	: Industry expected to perform in-line with the relevant broad market benchmark over next 12 months
UNDERPERFORM	: Industry expected to underperform the relevant broad market benchmark over next 12 months

CMB International Global Markets Limited

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

CMB International Global Markets Limited ("CMBIGM") is a wholly owned subsidiary of CMB International Capital Corporation Limited (a wholly owned subsidiary of China Merchants Bank)

Important Disclosures

There are risks involved in transacting in any securities. The information contained in this report may not be suitable for the purposes of all investors. CMBIGM does not provide individually tailored investment advice. This report has been prepared without regard to the individual investment objectives, financial position or special requirements. Past performance has no indication of future performance, and actual events may differ materially from that which is contained in the report. The value of, and returns from, any investments are uncertain and are not guaranteed and may fluctuate as a result of their dependence on the performance of underlying assets or other variable market factors. CMBIGM recommends that investors should independently evaluate particular investments and strategies, and encourages investors to consult with a professional financial advisor in order to make their own investment decisions.

This report or any information contained herein, have been prepared by the CMBIGM, solely for the purpose of supplying information to the clients of CMBIGM or its affiliate(s) to whom it is distributed. This report is not and should not be construed as an offer or solicitation to buy or sell any security or any interest in securities or enter into any transaction. Neither CMBIGM nor any of its affiliates, shareholders, agents, consultants, directors, officers or employees shall be liable for any loss, damage or expense whatsoever, whether direct or consequential, incurred in relying on the information contained in this report. Anyone making use of the information contained in this report does so entirely at their own risk.

The information and contents contained in this report are based on the analyses and interpretations of information believed to be publicly available and reliable. CMBIGM has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIGM provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIGM may issue other publications having information and/ or conclusions different from this report. These publications reflect different assumption, point-of-view and analytical methods when compiling. CMBIGM may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIGM may have a position, make markets or act as principal or engage in transactions in securities of companies referred to in this report for itself and/or on behalf of its clients from time to time. Investors should assume that CMBIGM does or seeks to have investment banking or other business relationships with the companies in this report. As a result, recipients should be aware that CMBIGM may have a conflict of interest that could affect the objectivity of this report and CMBIGM will not assume any responsibility in respect thereof. This report is for the use of intended recipients only and this publication, may not be reproduced, reprinted, sold, redistributed or published in whole or in part for any purpose without prior written consent of CMBIGM.

Additional information on recommended securities is available upon request.

For recipients of this document in the United Kingdom

This report has been provided only to persons (I)falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended from time to time)("The Order") or (II) are persons falling within Article 49(2) (a) to (d) ("High Net Worth Companies, Unincorporated Associations, etc.,) of the Order, and may not be provided to any other person without the prior written consent of CMBIGM.

For recipients of this document in the United States

CMBIGM is not a registered broker-dealer in the United States. As a result, CMBIGM is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. The research analyst who is primary responsible for the content of this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA"). The analyst is not subject to applicable restrictions under FINRA Rules intended to ensure that the analyst is not affected by potential conflicts of interest that could bear upon the reliability of the research report. This report is intended for distribution in the United States solely to "major US institutional investors", as defined in Rule 15a-6 under the US, Securities Exchange Act of 1934, as amended, and may not be furnished to any other person in the United States. Each major US institutional investor that receives a copy of this report by its acceptance hereof represents and agrees that it shall not distribute or provide this report to any other person. Any U.S. recipient of this report wishing to effect any transaction to buy or sell securities based on the information provided in this report should do so only through a U.S.-registered broker-dealer.

For recipients of this document in Singapore

This report is distributed in Singapore by CMBI (Singapore) Pte. Limited (CMBISG) (Company Regn. No. 201731928D), an Exempt Financial Adviser as defined in the Financial Advisers Act (Cap. 110) of Singapore and regulated by the Monetary Authority of Singapore. CMBISG may distribute reports produced by its respective foreign entities, affiliates or other foreign research houses pursuant to an arrangement under Regulation 32C of the Financial Advisers Regulations. Where the report is distributed in Singapore to a person who is not an Accredited Investor, Expert Investor or an Institutional Investor, as defined in the Securities and Futures Act (Cap. 289) of Singapore, CMBISG accepts legal responsibility for the contents of the report to such persons only to the extent required by law. Singapore recipients should contact CMBISG at +65 6350 4400 for matters arising from, or in connection with the report.