

CMBI Credit Commentary – XIAOMI

XIAOMI – Solid FY2021 result, tempered by its high spending appetite. Initiate Hold

Solid operating performance in 2021...

Reported FY2021 revenue of RMB 328bn and EBITDA of RMB 22.4bn, up 34% and 105% yoy. This was driven by its good smartphone shipment growth of 30% yoy in 2021, outperforming 5.7% global shipment growth during the period. Xiaomi maintained its global market share (14.1%) at No. 3 under tight chip supply. In 4Q21, Xiaomi resumed revenue growth to 21.4%yoy, from 8%yoy in 3Q21 despite chip shortage disruption.

... strength among all 3 segments

By segment, a) smartphone (64% of revenue) was a key performance driver, its sales rose 37%yoy to RMB 208.9bn and gross profit more than double to RMB 24.8bn, thanks to sales of more premium smartphone under chip shortage. b) IoT and lifestyle products (26% of revenue) grew 26% yoy to RMB 85bn and gross profit grew 29% yoy to RMB 11.1bn. c) Internet services (9% of revenue) also grew 19%yoy to RMB 28.2bn with gross profit of RMB 20.9bn.

Coupled with high capex and investment spending...

In 2021, Xiaomi remains in a high investment stage that it recorded capex of RMB7.2bn on top of RMB 13.1bn addition in long-term investments (i.e. ordinary shares and preferred shares in various companies in hardware supply chain and internet service), increasing its ending balance of long-term investments to RMB 50.5bn. As of Dec'21, Xiaomi's total debt increased to RMB26.2bn (from RMB 17.6bn as of Dec'20), representing Gross Debt/EBITDA of 1.2x (vs. 2020: 1.6x), but it still maintained a large net cash position thanks to its RMB 58.9bn total cash balance, and RMB31.7bn short-term investment.

Polly Ng 吴宝玲

(852) 3657 6234

pollyng@cmbi.com.hk

Glenn Ko, CFA 高志和

(852) 3657 6235

glennko@cmbi.com.hk

James Wen 温展俊

(852) 3757 6291

jameswen@cmbi.com.hk

CMBI Fixed Income

fis@cmbi.com.hk

Xiaomi is leveraging its operational strength as a hardware company to venture into internet services

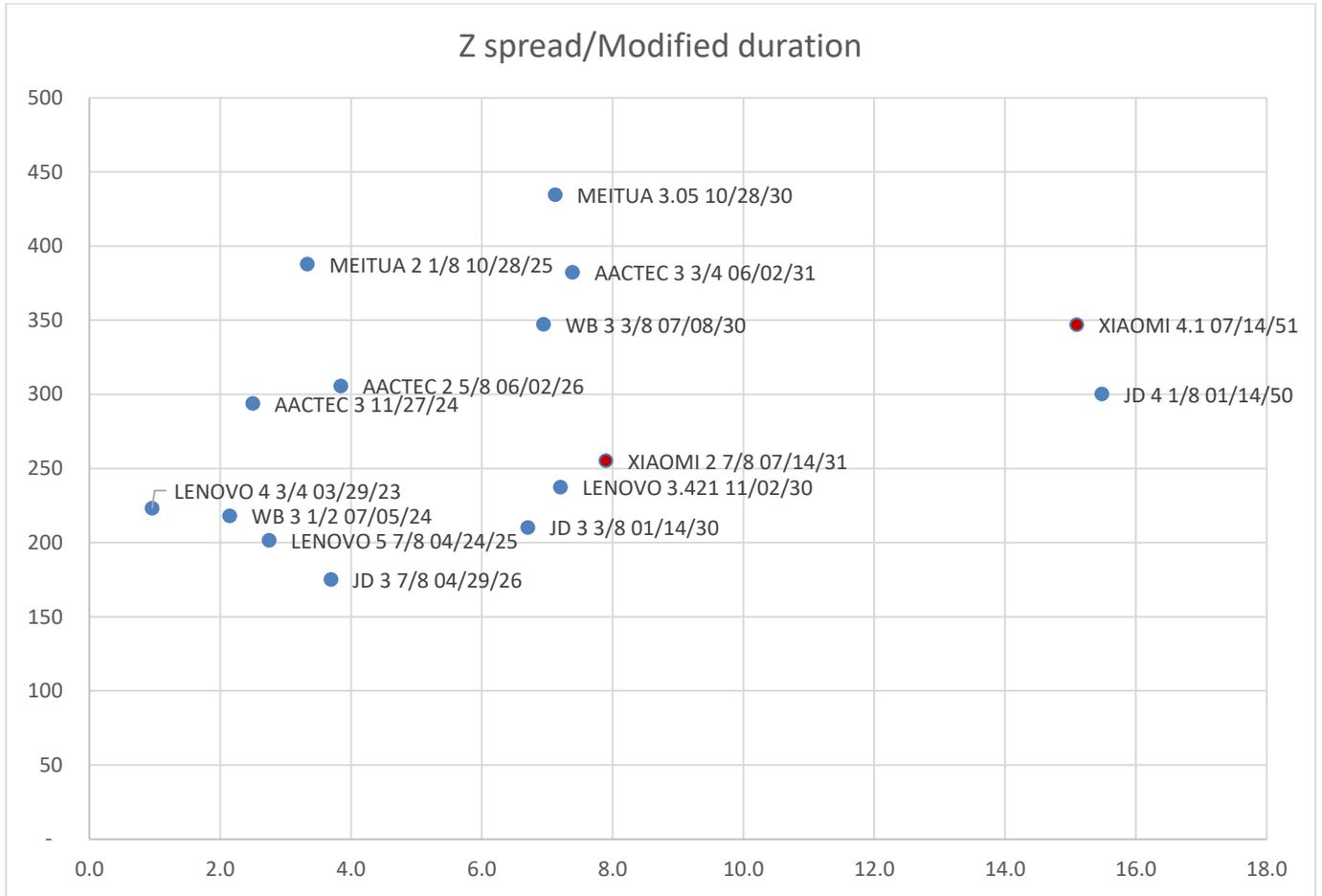
Xiaomi has been able to grow its internet service revenue at 19%-24% annual growth rate over the past 3 years, backed by its 28% annual growth of monthly active users globally (via its hardware sale). In 2021, 80% of Xiaomi's internet services revenue was derived from China, mostly via advertising to its domestic smartphone users. This segment contributes to over half of Xiaomi's EBITDA given its high gross margin of 74%, against low margin of its hardware products due to its competitive pricing strategy. However, regulation headwinds in China over data collection and usage might adversely affect Xiaomi's ability to monetize its domestic smartphone users in the future, in our view.

Xiaomi is committed to R&D and growth opportunities

Smartphone competition is fierce, especially given low brand loyalty for Android-based smartphones. To uphold its competitive position, Xiaomi plans to spend more than RMB 100bn in R&D over the next 5 years, vs. RMB 13.2bn (4% of revenue) spent in 2021. Moreover, Xiaomi's Electric Vehicle business plan, as a late-comer to the industry, will keep its capex high and increase its execution risk. We expect Xiaomi will generate negative discretionary cash flow in 2022, partly due to its share repurchase for shareholder's return. The company will maintain its share repurchase program to up to HKD 10bn (c.RMB 8.2bn) in 2022, vs. its total share buyback of RMB 7bn in 2021, to demonstrate confidence in its business outlook.

Valuation

We prefer LENOVO '30 at Z+237, compared to XIAOMI '31 at Z+255, given LENOVO's more disciplined investment track record and its gradual deleveraging trend. Hence we recommend Hold on XIAOMI at current valuation.



CMB International Securities Limited

Fixed Income Department

Tel: 852 3761 8867/ 852 3657 6291

fis@cmbi.com.hk

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