

ZTE (763 HK)

Strong growth in second-curve businesses

ZTE has announced 1Q25 results. Revenue increased by 8% YoY and 5% QoQ to RMB33.0bn, driven by strong revenue growth in enterprise/gov't segment (doubled YoY growth per mgmt.), benefitting from increased capex in compute infra. by leading domestic CSPs. NP decreased by 11% YoY to RMB2.5bn on a lower margin. GPM dropped YoY to 34.3% in 1Q25 vs. 42.0%/30.6% in 1Q24/4Q24, mainly due to an unfavourable product mix (higher revenue contribution from non-carrier business segments). **Maintain BUY as we view ZTE as a beneficiary in domestic AI market, with TP revised to RMB26.5.**

- **Second-curve businesses to drive future growth.** ZTE's second-curve businesses contributed over 35% of 1Q revenue, reflecting the company's strategic shift from "full connectivity" to a dual focus on "connectivity + computing power." Mgmt. highlighted enterprise/gov't segment revenue doubled YoY in 1Q25 and contributed over 20% of total sales (steadily increasing from 10.9%/15.3% in FY23/24), driven by strong domestic server demand. We project the segment sales to grow by 54% YoY in FY25, offsetting the impact from muted telcos' spending (China telcos' capex was down 9.7% in FY24 and is guided to decrease by another 9.1% in FY25, according to their own forecast). Overall, we forecast total revenue to increase by 10% YoY in FY25 (carrier sales estimated to decline 4% YoY while consumer and enterprise/gov't sales to grow by 15%/54% YoY).
- **Margin pressure from product mix shift.** ZTE's GPM declined by 7.8ppt in 1Q25 mainly on doubled enterprise/gov't sales (GPM: 15.3% in FY24) and weak carrier sales (GPM: 50.9% in FY24). While we expect server sales to remain a key growth driver in FY25, the shift in product mix could weigh on margins. We project FY25 GPM to be 36.7%. However, the impact on NPM should be more moderate as the company continues to enhance operational efficiency. We forecast FY25 NPM to be 6.7%, down 0.2ppt despite a 1.2ppt decline in GPM.
- **Maintain BUY with TP adjusted to RMB26.5, based on 13.2x 2025E P/E, which is 1 SD above its 2-year historical avg. (vs. prior 9.2x).** The higher multiple reflects ZTE's accelerating pivot toward AI-driven opportunities and the rapid growth of its second-curve businesses. Potential risks include: 1) China-US trade tensions, 2) softer capex of domestic telcos and overseas 5G deployment delays, 3) weaker-than-expected consumer or enterprise spending.

Earnings Summary

(YE 31 Dec)	FY23A	FY24A	FY25E	FY26E	FY27E
Revenue (RMB mn)	124,251	121,299	133,258	152,553	179,495
YoY growth (%)	1.1	(2.4)	9.9	14.5	17.7
Gross margin (%)	41.5	37.9	36.7	35.6	34.6
Net profit (RMB mn)	9,325.8	8,424.8	8,977.6	10,299.7	11,873.1
YoY growth (%)	15.4	(9.7)	6.6	14.7	15.3
P/E (x)	10.8	12.0	11.3	9.8	8.5
ROE (%)	14.7	12.0	11.8	12.5	13.2

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	HK\$26.50
(Previous TP)	HK\$22.43)
Up/Downside	18.3%
Current Price	HK\$22.40

China Semiconductors

Lily YANG, Ph.D

(852) 3916 3716

lilyyang@cmbi.com.hk

Kevin ZHANG

(852) 3761 8727

kevinzhang@cmbi.com.hk

Jiahao Jiang

(852) 39163739

JiangJiahao@cmbi.com.hk

Stock Data

Mkt Cap (HK\$ mn)	16,923.2
Avg 3 mths t/o (HK\$ mn)	1,048.0
52w High/Low (HK\$)	34.65/14.80
Total Issued Shares (mn)	755.5

Source: FactSet

Shareholding Structure

BlackRock	6.5%
Capital Group	5.1%

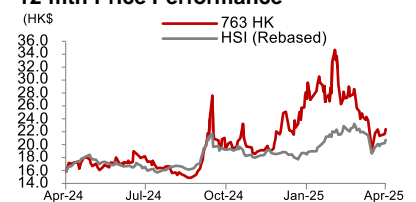
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	-12.7%	-6.3%
3-mth	-17.3%	-26.2%
6-mth	14.8%	7.9%

Source: FactSet

12-mth Price Performance



Source: FactSet

Figure 1: Earnings revision

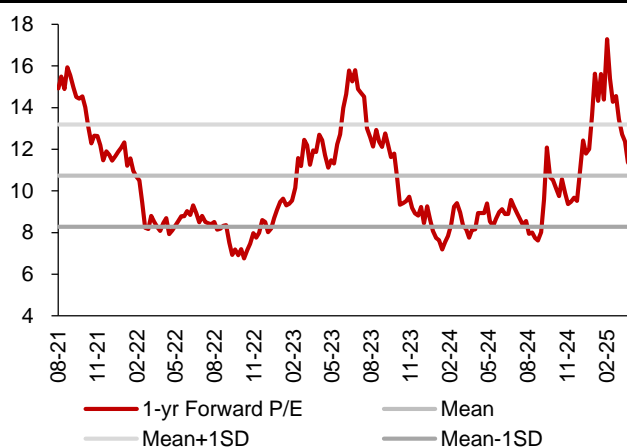
RMBmn	New			Old			Diff (%)		
	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
Revenue	133,258	152,553	179,495	133,471	146,541	NA	0%	4%	NA
Gross profit	48,969	54,286	62,178	52,321	56,711	NA	-6%	-4%	NA
Net profit	8,978	10,300	11,873	10,745	12,553	NA	-16%	-18%	NA
EPS (RMB)	1.88	2.15	2.48	2.25	2.62	NA	-17%	-18%	NA
Gross margin	36.7%	35.6%	34.6%	39.2%	38.7%	NA	-2.5 ppt	-3.1 ppt	NA
Net margin	6.7%	6.8%	6.6%	8.1%	8.6%	NA	-1.3 ppt	-1.8 ppt	NA

Source: Company data, CMBIGM estimates

Figure 2: CMBIGM estimates vs. Bloomberg consensus

RMBmn	CMBIGM			BBG Consensus			Diff (%)		
	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
Revenue	133,258	152,553	179,495	131,942	142,175	153,686	1%	7%	17%
Gross profit	48,969	54,286	62,178	50,259	53,363	55,558	-3%	2%	12%
Net profit	8,978	10,300	11,873	9,635	10,373	10,860	-7%	-1%	9%
EPS (RMB)	1.88	2.15	2.48	2.00	2.17	2.23	-6%	-1%	11%
Gross margin	36.7%	35.6%	34.6%	38.1%	37.5%	36.2%	-1.3 ppt	-1.9 ppt	-1.5 ppt
Net margin	6.7%	6.8%	6.6%	7.3%	7.3%	7.1%	-0.6 ppt	-0.5 ppt	-0.5 ppt

Source: Bloomberg, CMBIGM estimates

Figure 3: P/E band

Source: Bloomberg, CMBIGM estimates

Figure 4: P/E chart

Source: Bloomberg, CMBIGM estimates

Financial Summary

INCOME STATEMENT	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec (RMB mn)						
Revenue	122,954	124,251	121,299	133,258	152,553	179,495
Cost of goods sold	(77,228)	(72,650)	(75,311)	(84,289)	(98,267)	(117,316)
Gross profit	45,727	51,601	45,988	48,969	54,286	62,178
Operating expenses	(35,166)	(40,623)	(35,652)	(37,735)	(41,967)	(48,302)
Selling expense	(9,173)	(10,172)	(8,901)	(9,112)	(9,973)	(11,376)
Admin expense	(5,333)	(5,632)	(4,477)	(4,585)	(4,944)	(5,458)
SG&A expense	(951)	(1,336)	(1,176)	(1,292)	(1,479)	(1,740)
R&D expense	(21,602)	(25,289)	(24,031)	(26,001)	(29,384)	(34,215)
Others	1,893	1,806	2,933	3,255	3,814	4,487
Operating profit	10,561	10,978	10,335	11,234	12,318	13,876
Other income	196	173	76	84	96	113
Other expense	(239)	(228)	(189)	(207)	(238)	(279)
Gain/loss on financial assets at FVTPL	(1,142)	(702)	(625)	0	0	0
Investment gain/loss	1,087	(205)	112	0	0	0
Other gains/(losses)	(1,548)	(914)	(745)	(1,190)	(1,245)	(1,302)
EBIT	8,915	9,102	8,965	9,920	10,932	12,408
Net Interest income/(expense)	(163)	1,101	265	(84)	352	599
Other income/expense	(657)	158	(687)	0	0	0
Pre-tax profit	8,752	10,203	9,230	9,835	11,284	13,007
Income tax	(960)	(962)	(874)	(931)	(1,068)	(1,232)
After tax profit	7,792	9,241	8,356	8,904	10,215	11,776
Minority interest	(289)	(85)	(69)	(74)	(85)	(97)
Others	0	0	0	0	0	0
Net profit	8,080	9,326	8,425	8,978	10,300	11,873
BALANCE SHEET	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec (RMB mn)						
Current assets	137,874	158,505	141,787	152,902	160,579	168,679
Cash & equivalents	47,072	51,013	28,027	35,579	38,622	40,108
Restricted cash	9,274	27,530	15,859	10,608	10,608	10,608
Account receivables	19,098	21,968	23,886	25,766	27,732	29,313
Inventories	45,235	41,131	41,258	45,572	47,042	50,668
Prepayment	279	242	692	396	521	573
Financial assets at FVTPL	514	153	13,769	15,697	16,393	17,238
Other current assets	16,402	16,466	18,297	19,283	19,661	20,170
Non-current assets	43,080	42,454	65,536	68,269	70,405	74,213
PP&E	13,877	14,360	14,178	14,040	13,783	13,468
Right-of-use assets	1,080	1,557	1,552	1,503	1,440	1,377
Deferred income tax	3,719	4,146	4,396	4,321	4,513	4,746
Intangibles	9,926	8,999	7,159	6,504	6,375	6,746
Goodwill	0	0	14	15	15	16
Financial assets at FVTPL	1,028	832	716	777	777	777
Other non-current assets	13,450	12,559	37,520	41,109	43,502	47,083
Total assets	180,954	200,958	207,323	221,171	230,984	242,892
Current liabilities	78,424	83,030	82,635	100,635	103,900	103,780
Short-term borrowings	9,962	7,560	7,027	15,095	15,320	10,070
Account payables	32,595	32,219	36,568	44,804	46,546	50,100
Tax payable	1,447	1,413	1,205	1,590	1,661	1,747
Other current liabilities	3,498	10,771	7,984	13,493	13,583	13,692
Contract liabilities	30,922	31,067	29,851	25,652	26,791	28,172
Non-current liabilities	42,987	49,596	51,577	41,501	40,978	44,839
Long-term borrowings	35,126	42,576	44,059	32,659	31,834	35,327
Bond payables	0	0	1,005	2,012	2,012	2,012
Obligations under finance leases	789	960	973	975	1,018	1,071
Deferred income	87	78	91	90	94	99
Other non-current liabilities	6,985	5,982	5,450	5,765	6,020	6,331
Total liabilities	121,410	132,627	134,213	142,135	144,879	148,619
Share capital	4,736	4,783	4,784	4,784	4,784	4,784
Capital surplus	0	0	0	0	0	0
Retained earnings	27,309	34,715	39,873	45,899	53,053	61,318
Other reserves	26,596	28,510	28,152	28,125	28,125	28,125
Total shareholders equity	58,641	68,008	72,808	78,808	85,962	94,227
Minority interest	902	323	302	228	144	46
Total equity and liabilities	180,954	200,958	207,323	221,171	230,984	242,892

CASH FLOW	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	7,792	9,241	8,356	8,904	10,215	11,776
Depreciation & amortization	4,386	4,926	4,969	5,505	5,901	12,273
Tax paid	(587)	(437)	(237)	74	(188)	(416)
Change in working capital	(8,471)	(324)	(2,505)	735	(2,329)	(5,521)
Others	4,458	3,999	898	51	5,728	5,951
Net cash from operations	7,578	17,406	11,480	15,270	19,328	24,064
Investing						
Capital expenditure	(4,952)	(4,005)	(4,015)	(6,745)	(7,474)	(8,473)
Acquisition of subsidiaries/ investments	3,636	(17,001)	(25,299)	(1,930)	(702)	(851)
Net proceeds from disposal of short-term investments	24	104	535	581	616	658
Others	(471)	(635)	(415)	3,502	(1,190)	(1,444)
Net cash from investing	(1,762)	(21,536)	(29,193)	(4,592)	(8,749)	(10,110)
Financing						
Dividend paid	(3,688)	(4,836)	(5,419)	(6,650)	(6,936)	(7,326)
Net borrowings	5,442	11,164	(253)	3,552	(600)	(1,758)
Proceeds from share issues	171	1,676	374	(27)	0	0
Others	(471)	(633)	(521)	0	0	0
Net cash from financing	1,455	7,372	(5,818)	(3,126)	(7,536)	(9,083)
Net change in cash						
Cash at the beginning of the year	39,071	47,072	51,013	28,027	35,579	38,622
Exchange difference	260	66	24	0	0	0
Others	7,741	3,876	(23,011)	7,553	3,042	1,486
Cash at the end of the year	47,072	51,013	28,027	35,579	38,622	40,108
GROWTH	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec						
Revenue	7.4%	1.1%	(2.4%)	9.9%	14.5%	17.7%
Gross profit	13.3%	12.8%	(10.9%)	6.5%	10.9%	14.5%
Operating profit	23.7%	4.0%	(5.9%)	8.7%	9.7%	12.6%
EBIT	(5.8%)	2.1%	(1.5%)	10.6%	10.2%	13.5%
Net profit	18.6%	15.4%	(9.7%)	6.6%	14.7%	15.3%
PROFITABILITY	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec						
Gross profit margin	37.2%	41.5%	37.9%	36.7%	35.6%	34.6%
Operating margin	8.6%	8.8%	8.5%	8.4%	8.1%	7.7%
Return on equity (ROE)	14.7%	14.7%	12.0%	11.8%	12.5%	13.2%
GEARING/LIQUIDITY/ACTIVITIES	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec						
Current ratio (x)	1.8	1.9	1.7	1.5	1.5	1.6
VALUATION	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec						
P/E	12.4	10.8	12.0	11.3	9.8	8.5
P/E (diluted)	12.4	10.8	12.0	11.3	9.8	8.5

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

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CMB International Global Markets Limited

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

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