

Jiangsu Hengli Hydraulic (601100 CH)

Revenue rebounded in 3Q22; Wait for more data points to confirm recovery

Hengli's reported net profit in 3Q22 grew 20% YoY, driven by FX gain due to the strong dollar. We estimate the core profit (excluding the finance income arising from FX gain) dropped ~9% YoY in 3Q22. While the 4% YoY revenue growth (vs -25% YoY in 1H22) is an early sign of recovery, it's still slightly below our expectation. We revise down our 2022E/23E earnings forecast by 9%/8% to reflect more conservative assumptions on sales volume. We trim our TP to RMB58 accordingly, based on unchanged 30x 2022E P/E (equivalent to 3-year historical average). Maintain **HOLD**. We believe we are close to the inflection point but are waiting for more data points to confirm the recovery of excavator sales.

- **3Q22 earnings highlights.** Revenue grew 4% YoY to RMB2bn, which we estimate was driven by the strong sales to the major US customer. Gross margin narrowed 2.1ppt YoY but expanded 1.7ppt QoQ. EBIT slightly dropped 1.6% YoY to RMB576mn. It's worth noting that Hengli recognized net finance income of RMB170mn (vs RMB6mn in 3Q21), thanks to the appreciation of dollar-denominated assets. This boosted the reported net profit by 20% YoY to RMB692mn. Operating cash inflow dropped 59% YoY to RMB377mn in 3Q22. In 9M22, the reported net profit dropped 11% YoY to RMB1.75bnn.
- **Production plan in Oct 2022:** Hengli has scheduled production volume of 56k units of hydraulic cylinder (excavator), down ~15% YoY. Scheduled production volume of small /medium-large size pump drops >50% YoY, as a result of the continuous inventory clearance that affected the output. Planned volume of motor (mainly for AWP) drops 15% YoY. On the positive side, the planned production for non-standardized cylinders in Oct grows 7% YoY to 16k units.
- **Early signs of recovery for the excavator industry.** For the industry as a whole, we have started to see some early positive signs: (1) strong export will likely exceed expectation on the back of overseas mining activities; (2) upcoming sales data points in China will potentially beat expectations on the back of the very low base and continuous policy easing; (3) major cost items such as steel plate and freight rate are on the down trend, offering upside potential on the margin side.
- **Upside risk:** (1) Strong recovery of excavator demand in China. **Downside risks:** (1) weak construction activities; (2) risk of overseas demand.

Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (RMB mn)	7,855	9,309	8,378	9,008	9,714
YoY growth (%)	45.1	18.5	-10.0	7.5	7.8
Net income (RMB mn)	2,254	2,694	2,536	2,844	3,137
EPS (RMB)	1.73	2.06	1.94	2.18	2.40
YoY growth (%)	73.9	19.5	-5.9	12.2	10.3
Consensus EPS (RMB)	NA	NA	1.87	2.15	2.58
EV/EBITDA (x)	21.6	19.0	23.1	19.9	18.6
P/E (x)	30.0	25.1	26.7	23.8	21.5
P/B (x)	9.2	7.4	6.3	5.3	4.5
Yield (%)	1.2	1.4	1.3	1.5	1.6
ROE (%)	35.0	32.6	25.4	24.2	22.7
Net debt / equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIGM estimates

HOLD (Maintain)

Target Price: **RMB58.00**
 (Previous TP **RMB64.00**)
 Up/Downside: **12%**
 Current Price: **RMB51.78**

China Capital Goods

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Stock Data

Mkt Cap (RMB mn)	67,592
Avg 3 mths t/o (RMB mn)	262.19
52w High/Low (RMB)	90.67/41.08
Total Issued Shares (mn)	1,305

Source: Bloomberg

Shareholding Structure

WANG's family	71.0%
CCASS (Hong Kong)	10.0%
Others	19.0%

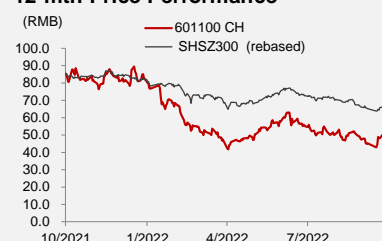
Source: Company data

Share Performance

	Absolute	Relative
1-mth	9.1%	12.4%
3-mth	-6.0%	6.4%
6-mth	13.8%	22.0%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: RSM

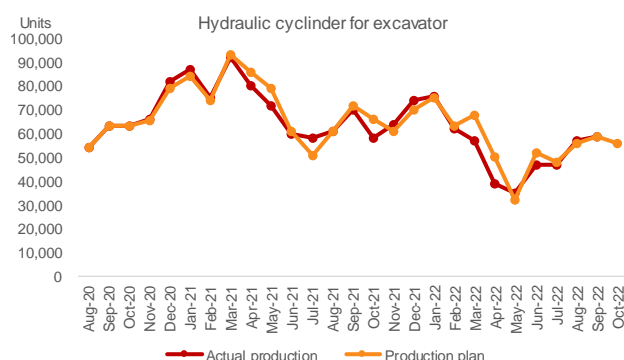
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Figure 1: 3Q22 results highlights

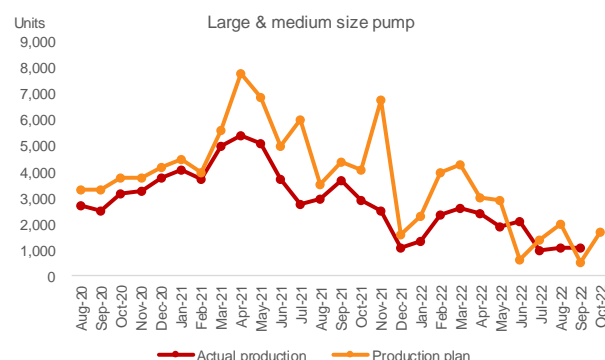
(RMB mn)	1Q21	1Q22	Change YoY	2Q21	2Q22	Change YoY	3Q21	3Q22	Change YoY
Total revenue	2,857	2,200	-23.0%	2,370	1,686	-28.9%	1,956	2,033	4.0%
Cost of sales	-1,684	-1,367	-18.8%	-1,398	-998	-28.6%	-1,083	-1,168	7.8%
Gross profit	1,172	833	-28.9%	972	688	-29.2%	872	865	-0.9%
Other income	-30	-21	-28.2%	-17	-14	-18.1%	-14	-16	11.7%
S&D expenses	-30	-23	-21.9%	-16	-19	20.0%	-16	-32	95.7%
Administrative expenses	-168	-170	1.3%	-188	-246	31.1%	-305	-267	-12.3%
Asset impairment	-23	-8	-66.5%	11	8	-27.3%	48	26	-45.9%
EBIT	922	611	-33.8%	763	417	-45.3%	585	576	-1.6%
Net finance income/(cost)	-2	-20	806.9%	-39	183	n/a	6	170	2700.2%
Other gains/(loss)	18	28	61.6%	20	18	-6.1%	-0	-12	2414.9%
Profit of JV & associates	0	0	n/a	0	0	n/a	0	0	n/a
Pretax profit	937	619	-33.9%	744	618	-16.9%	591	734	24.2%
Income tax	-153	-90	-41.3%	-116	-88	-23.9%	-13	-41	215.7%
After tax profit	784	529	-32.5%	628	530	-15.6%	578	694	20.0%
MI	-1	-1	-16.3%	-2	-1	-45.7%	-1	-1	10.1%
Net profit	783	528	-32.5%	626	529	-15.5%	577	692	20.0%

Key ratios			ppt			ppt			ppt
Gross margin	41.0%	37.9%	-3.2	41.0%	40.8%	-0.2	44.6%	42.5%	-2.1
S&D expense ratio	1.0%	1.0%	0.0	0.7%	1.2%	0.5	0.8%	1.6%	0.7
Administrative and R&D exp ratio	5.9%	7.7%	1.9	7.9%	14.6%	6.7	15.6%	13.1%	-2.4
Effective tax rate	16.4%	14.5%	-1.8	15.6%	14.2%	-1.3	2.2%	5.5%	3.4

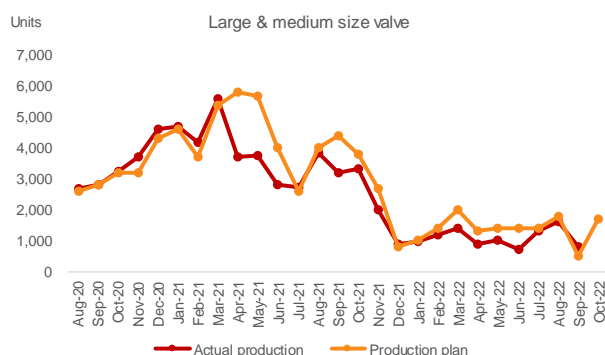
Source: Company data, CMBIGM estimates

Figure 2: Hengli's hydraulic cylinders monthly production

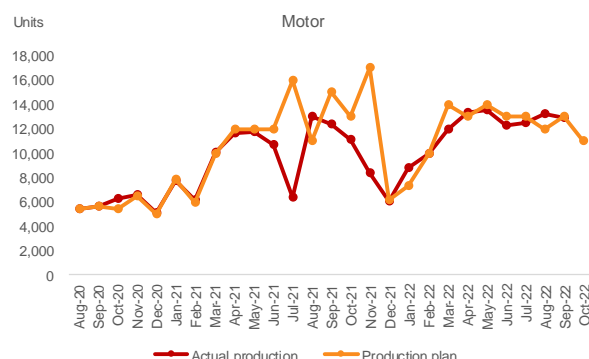
Source: Company data, CMBIGM estimates

Figure 3: Hengli's large & medium size pump monthly production

Source: Company data, CMBIGM estimates

Figure 4: Hengli's large & medium size valve monthly production

Source: Company data, CMBIGM estimates

Figure 5: Hengli's motor monthly production

Source: Company data, CMBIGM estimates

Figure 6: Change in key assumptions and earnings

(RMB mn)	Old			New			Change		
	2022E	2023E	2024E	2022E	2023E	2024E	2022E	2023E	2024E
Revenue (hydraulic business)	9,939	10,554	-	8,349	8,975	9,677	-16.0%	-15.0%	-
Other business	30	32	-	29	33	37	-4.1%	5.0%	-
Total revenue	9,969	10,586	-	8,378	9,008	9,714	-16.0%	-14.9%	-
Gross margin									
Hydraulic cylinder	41.5%	41.0%	-	41.5%	43.1%	42.8%	0.0	2.1	-
Hydraulic pump and valve	42.0%	42.0%	-	45.0%	47.0%	47.0%	3.0	5.0	-
Gross margin (hydraulic business)	39.4%	39.3%	-	41.2%	42.9%	42.8%	1.8	3.6	-
Other business	90.0%	90.0%	-	90.0%	90.0%	74.0%	0.0	0.0	-
Blended gross margin	39.6%	39.5%	-	41.4%	43.1%	42.9%	1.8	3.6	-
							Change (ppt)		
S&D expense ratio	-0.8%	-0.8%	-	-1.5%	-1.5%	-1.5%	-0.7	-0.7	-
Admin expense and R&D ratio	-8.5%	-8.5%	-	-10.3%	-9.5%	-9.5%	-1.8	-1.0	-
Net profit	2,795	3,090	-	2,536	2,844	3,137	-9.3%	-7.9%	-

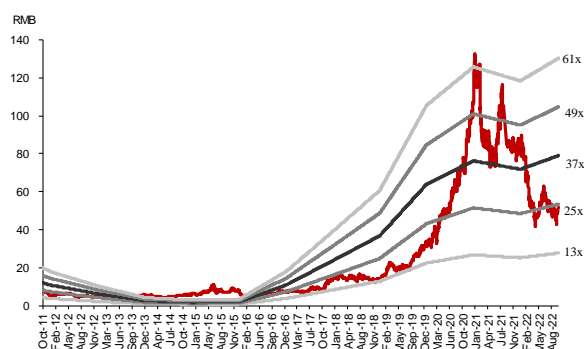
Source: Company data, CMBIGM estimates

Figure 7: Key assumptions

(RMB mn)	2020	2021	2022E	2023E	2024E
Revenue					
Hydraulic cylinder	4,497	5,187	4,930	5,278	5,592
Hydraulic pump and valve	2,338	3,236	2,940	3,165	3,504
Hydraulic system	157	196	108	116	122
Component	845	677	372	417	459
Revenue (hydraulic business)	7,838	9,295	8,349	8,975	9,677
Other business	17	14	29	33	37
Total revenue	7,855	9,309	8,378	9,008	9,714
Revenue growth					
Hydraulic cylinder	27.0%	15.3%	-5.0%	7.1%	6.0%
Hydraulic pump and valve	85.2%	38.4%	-9.1%	7.7%	10.7%
Hydraulic system	82.9%	25.1%	-45.0%	7.0%	6.0%
Component	68.8%	-20.0%	-45.0%	12.0%	10.0%
Revenue (hydraulic business)	45.4%	18.6%	-10.2%	7.5%	7.8%
Other business	-23.1%	-19.6%	110.0%	15.0%	10.0%
Total revenue	45.1%	18.5%	-10.0%	7.5%	7.8%
Gross margin					
Hydraulic cylinder	46.8%	44.2%	41.5%	43.1%	42.8%
Hydraulic pump and valve	52.3%	52.0%	45.0%	47.0%	47.0%
Hydraulic system	45.7%	45.2%	45.0%	45.5%	45.5%
Component	6.2%	3.5%	6.0%	10.0%	11.0%
Gross margin (hydraulic business)	44.0%	44.0%	41.2%	42.9%	42.8%
Other business	74.3%	70.9%	90.0%	90.0%	74.0%
Blended gross margin	44.1%	44.0%	41.4%	43.1%	42.9%

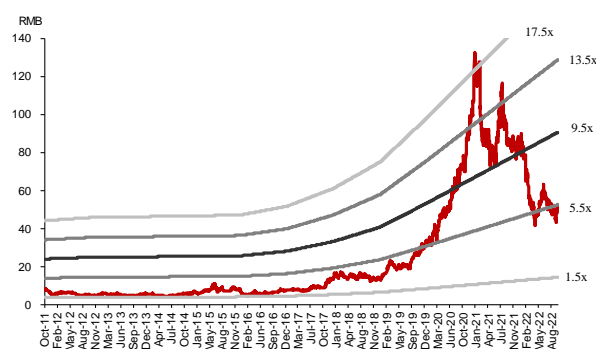
Source: Company data, CMBIGM estimates

Figure 8: Hengli's P/E band



Source: Bloomberg, Company data, CMBIGM estimates

Figure 9: Hengli's P/B band



Source: Bloomberg, Company data, CMBIGM estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Total revenue	7,855	9,309	8,378	9,008	9,714
Cost of sales	-4,391	-5,211	-4,911	-5,124	-5,543
Gross profit	3,464	4,098	3,467	3,884	4,171
Surcharge	-72	-78	-67	-72	-78
S&D expenses	-107	-112	-126	-135	-146
Administrative expenses	-509	-863	-863	-856	-923
Asset impairment	-90	-47	-50	-50	-50
EBIT	2,687	2,998	2,361	2,771	2,975
Net finance income/(cost)	-151	-89	442	377	499
Finance income	223	246	498	437	535
Finance expenses	-375	-335	-56	-60	-36
Other gains/(losses)	74	160	84	90	97
Profit of JV and associates	0	0	0	0	0
Pretax profit	2,609	3,069	2,887	3,238	3,572
Income tax	-348	-369	-346	-389	-429
After tax profit	2,261	2,700	2,541	2,850	3,143
MI	-7	-5	-5	-6	-6
Net profit	2,254	2,694	2,536	2,844	3,137
D&A	311	404	436	473	497
EBITDA	2,997	3,402	2,798	3,244	3,472

Cash flow summary

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Pretax profit	2,609	3,069	2,887	3,238	3,572
Finance cost	146	86	56	60	36
Profit or loss of associates	0	0	0	0	0
Loss/(gain) on disposal	1	1	0	0	0
Depreciation & amortization	311	404	436	473	497
Income tax paid	-714	-369	-346	-389	-429
Change in working capital	-849	-472	272	-156	-1,110
Others	488	84	0	0	0
Cash flow from operation	1,981	2,796	3,305	3,227	2,566
Net capex on PP&E	-380	-558	-600	-600	-400
Investment in JV/associates	0	0	0	0	0
Investment in subsidiaries	0	0	0	0	0
Investment in intangibles	-19	-4	-20	-20	0
Dividend received	0	0	0	0	0
Others	-264	-371	0	0	0
Cash flow from investing	-663	-932	-620	-620	-400
Equity financing/(repurchase)	0	0	0	0	0
Net bank borrowings	-361	-287	100	0	0
Dividend paid	-529	-783	-953	-888	-995
Interest paid	-40	18	-56	-60	-36
Others	112	339	0	0	0
Cash flow from financing	-818	-714	-909	-948	-1,031
Change in cash	499	1,150	1,776	1,660	1,135
Cash at beginning of the year	2,343	2,777	3,643	5,419	7,079
Exchange and others	-66	-284	0	0	0
Cash at the end of the year	2,777	3,643	5,419	7,079	8,214

Balance sheet

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Non-current assets	3,025	3,186	3,370	3,517	3,420
PP&E	2,432	2,580	2,757	2,898	2,815
JV/associates	0	0	0	0	0
Goodwill	0	0	0	0	0
Intangible assets	280	267	273	279	265
AFS investments	0	0	0	0	0
Others	261	289	289	289	289
Deferred tax assets	52	50	50	50	50
Current assets	7,595	9,146	10,454	12,560	14,730
Inventories	1,217	1,607	1,300	1,508	2,440
Trade and bill receivables	2,705	2,560	2,398	2,636	2,739
Prepayment	164	160	160	160	160
Others	733	1,177	1,177	1,177	1,177
Pledged deposits	0	0	0	0	0
Cash	2,777	3,643	5,419	7,079	8,214
Current liabilities	2,590	2,691	2,595	2,885	2,811
Trade and bill payables	1,131	1,188	992	1,282	1,208
Bank borrowings	554	597	697	697	697
Tax payable	119	84	84	84	84
Advance from customers	108	39	39	39	39
Others	677	783	783	783	783
Non-current liabilities	679	402	402	402	402
Bank borrowings	370	44	44	44	44
Deferred tax liabilities	108	147	147	147	147
Deferred income	200	204	204	204	204
Others	0	6	6	6	6
Equity	7,352	9,239	10,827	12,790	14,937
Shareholders' equity	7,314	9,196	10,779	12,735	14,876
MI	38	44	49	54	61

Key ratios

YE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Sales mix (%)					
Hydraulic cylinder	57%	56%	59%	59%	58%
Hydraulic pump and valve	30%	35%	35%	35%	36%
Hydraulic system	2%	2%	1%	1%	1%
Component	11%	7%	4%	5%	5%
Other business	0%	0%	0%	0%	0%
Total revenue	100%	100%	100%	100%	100%
Profit & loss ratio (%)					
Gross margin	44.1	44.0	41.4	43.1	42.9
EBIT margin	34.2	32.2	28.2	30.8	30.6
Net profit margin	28.8	29.0	30.3	31.6	32.4
Growth (%)					
Revenue	45.1	18.5	-10.0	7.5	7.8
Gross profit	69.4	18.3	-15.4	12.0	7.4
EBIT	92.7	11.6	-21.2	17.4	7.4
Net profit	73.9	19.5	-5.9	12.2	10.3
Balance sheet ratio					
Current ratio (x)	2.9	3.4	4.0	4.4	5.2
Receivable turnover days	101	103	108	102	101
Inventory turnover days	92	99	108	100	130
Payable turnover days	80	81	81	81	82
Net debt / total equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Profitability (%)					
ROA	23.7	23.5	19.4	19.0	18.3
ROE	35.0	32.6	25.4	24.2	22.7
Per share data					
EPS (RMB)	1.73	2.06	1.94	2.18	2.40
BVPS (RMB)	5.60	7.04	8.26	9.76	11.40
DPS (RMB)	0.60	0.73	0.68	0.76	0.84

Source: Company data, CMBIGM estimates

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