

Zoomlion Heavy Industry - A (000157 CH)

Margin risk priced in; Good buying opportunity

Zoomlion's 3Q20 profit is solid (+85% YoY) and management's post-results comments on demand (+10% QoQ in 4Q20E) and margin (to improve sequentially) suggest that the business outlook remains favourable. We believe the recent share price pullback on concerns over margin was overdone and we see this as good buying opportunity. We slightly took our 2020E-22E earnings forecast down by 2-4% after modelling higher sales volume but more conservative margins. We fine-tuned our TP from RMB10.2 to RMB9.56, after rolling over our base year to 2021E with a target multiple of 10x (previously 12x 2020E P/E). Maintain **BUY**.

- Key highlight on 3Q20 results.** Net profit in 3Q20 surged 85% YoY to RMB1.67bn, within the range of profit alert (RMB1.48-1.78bn) released in mid-Oct. Revenue grew 73% YoY to RMB16.4bn while gross margin narrowed 2.4ppt YoY and 1.8ppt QoQ to 27%. Net operating cash inflow increased by 58% YoY to RMB2.6bn in 3Q.
- Strong growth across all segments.** In 9M20, concrete machinery and crane revenue increased by 34% YoY and 44% YoY, respectively, to RMB13.7bn and RMB23.6bn. Agricultural machinery revenue grew 35% YoY. For new business lines, revenue from excavator surged 244% YoY while revenue from aerial working platform (AWP) grew 60% YoY.
- Gross margin to rebound in 4Q20E.** Gross margin contraction in 3Q20 was due to: (1) higher sales of smaller size truck cranes and tower crane that carried lower margin; (2) higher growth of concrete mixer (lower margin) than the concrete pump; (3) fast growing AWP and excavator which had lower margin (though improving), compared with the existing business. That said, management is confident of achieving better margin in 4Q20E, as (1) new business margin keeps improving, and (2) the Company's central procurement policy started in 3Q20 will help reduce cost going forward.
- Positive outlook in 4Q20E and 2021E.** Management believes that solid infrastructure and property investment, together with the replacement of labour and strict environmental protection policies are all favourable drivers. Besides, large players are beneficiaries of rising industry concentration. Management believes that this round of upcycle will be stronger than the previous one.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	28,697	43,307	63,942	76,025	84,903
YoY growth (%)	39.3	50.9	47.6	18.9	11.7
Net income (RMB mn)	2,031	4,381	6,887	8,727	9,928
EPS (RMB)	0.27	0.58	0.87	0.96	1.09
YoY growth (%)	51.5	119.2	50.0	9.3	13.7
Consensus EPS (RMB)	n/a	n/a	0.82	0.92	1.02
EV/EBITDA (x)	16.0	10.5	7.9	6.5	5.8
P/E (x)	27.0	12.6	8.7	7.9	6.8
P/B (x)	1.5	1.5	1.3	1.2	1.0
Yield (%)	3.5	0.0	4.9	5.1	5.9
ROE (%)	5.4	11.4	16.3	16.8	16.1
Net gearing (%)	33.6	31.3	20.8	4.7	3.6

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

Target Price	RMB9.56
(Previous TP	RMB10.20)
Up/Downside	+32%
Current Price	RMB7.24

China Capital Goods

Wayne Fung, CFA
 (852) 3900 0826
 waynefung@cmbi.com.hk

Stock Data

Mkt Cap (RMB mn)	55,697
Avg 3 mths t/o (RMB mn)	468
52w High/Low (RMB)	8.97/5.28
Total Issued Shares (mn)	6,411 (A)
	1,388 (H)

Source: Bloomberg

Shareholding Structure

SASAC of Hunan Province	15.9%
Management team	4.9%
A share free float	61.4%
H share free float	17.7%

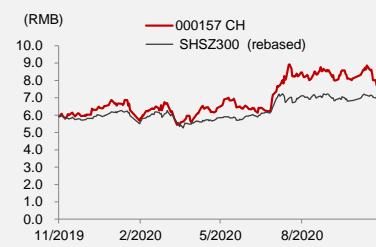
Source: HKEx, Shanghai Stock Exchange

Share Performance

	Absolute	Relative
1-mth	-8.8%	-10.9%
3-mth	-10.4%	-10.4%
6-mth	15.6%	-3.7%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: KPMG

Related Reports

- Zoomlion (000157 CH, BUY) – Profit surprise in 3Q20 reaffirms our positive view – 15 Oct 2020
- Zoomlion (000157 CH, BUY) – Interim dvd. a positive; Gross margin stabilized; Sector top pick – 24 Aug 2020
- Zoomlion (000157 CH, BUY) – 2Q20 profit a strong beat; Lift earnings est. & TP – 15 Jul 2020
- China Construction Machinery & HDT Sector – Raise industry sales forecast in 2020E-21E; Solid upcycle – 30 Jun 2020

Figure 1: 3Q20 results highlights

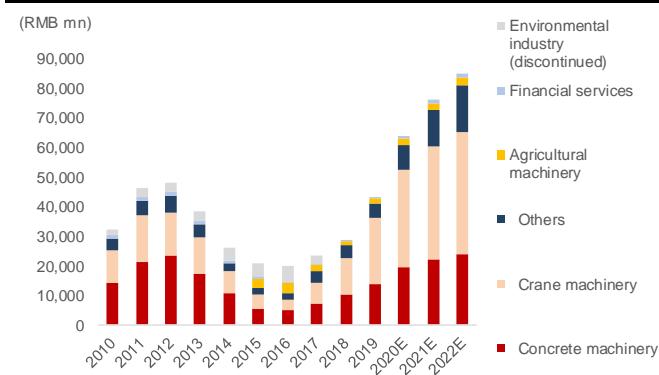
(RMB mn)	1Q19	1Q20	Change YoY	2Q19	2Q20	Change YoY	3Q19	3Q20	Change YoY
Total revenue	9,017	9,067	0.6%	13,245	19,760	49.2%	9,493	16,417	72.9%
Cost of sales	-6,311	-6,296	-0.2%	-9,273	-14,068	51.7%	-6,702	-11,979	78.7%
Gross profit	2,706	2,770	2.4%	3,972	5,693	43.3%	2,791	4,438	59.0%
Other income	29	114	289.3%	593	548	-7.6%	200	7	-96.6%
S&D expenses	-715	-704	-1.5%	-1,166	-1,212	3.9%	-890	-1,223	37.5%
Administrative expenses	-624	-488	-21.7%	-1,045	-1,782	70.5%	-535	-1,000	86.8%
R&D expenses	-116	-242	108.9%	-345	-806	133.5%	-270	-662	145.3%
EBIT	1,281	1,450	13.3%	2,353	3,247	38.0%	1,295	1,559	20.3%
Net finance income/(cost)	-405	-280	-30.8%	-191	243	n/a	-301	20	n/a
Other gains/(losses)	234	69	-70.7%	-234	-69	-70.7%	99	242	143.8%
Share of profit of JV and associates	34	47	40.7%	48	19	-61.2%	40	42	4.9%
Pretax profit	1,144	1,286	12.5%	1,976	3,440	74.1%	1,134	1,863	64.3%
Income tax	-162	-236	45.3%	-378	-432	14.4%	-245	-178	-27.2%
After tax profit	981	1,050	7.0%	1,599	3,008	88.1%	889	1,685	89.4%
MI	21	-24	n/a	-16	-9	n/a	14	-17	n/a
Net profit	1,002	1,026	2.4%	1,583	2,999	89.5%	904	1,668	84.6%
Operating cash flow	1,867	319	-82.9%	1,431	1,068	-25.4%	1,664	2,630	58.0%
Key ratios			Change (ppt)			Change (ppt)			Change (ppt)
<i>Gross margin</i>	30.0%	30.6%	0.5	30.0%	28.8%	-1.2	29.4%	27.0%	-2.4
<i>S&D expenses ratio</i>	7.9%	7.8%	-0.2	8.8%	6.1%	-2.7	9.4%	7.5%	-1.9
<i>Administrative expense ratio</i>	6.9%	5.4%	-1.5	7.9%	9.0%	1.1	5.6%	6.1%	0.5
<i>R&D expense ratio</i>	1.3%	2.7%	1.4	2.6%	4.1%	1.5	2.8%	4.0%	1.2
<i>Net margin</i>	10.9%	11.6%	0.7	12.1%	15.2%	3.2	9.4%	10.3%	0.9
<i>Effective tax rate</i>	14.2%	18.3%	4.1	19.1%	12.6%	-6.5	21.6%	9.6%	-12.0

Source: Company data, CMBIS

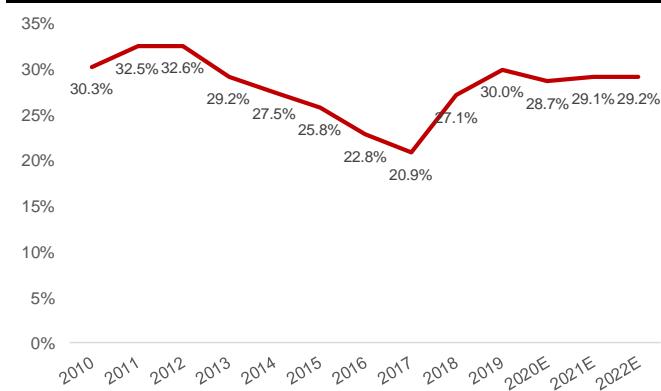
Figure 2: Change in key assumptions

	Old	2020E	2021E	2022E	New	2020E	2021E	2022E	Change	2021E	2022E
		2020E	2021E	2022E		2020E	2021E	2022E	2021E	2022E	
(RMB mn)											
Revenue											
Construction machinery	56,223	66,924	75,810	60,946	72,608	81,097	8%	8%	7%		
Concrete machinery	17,656	20,304	22,334	19,324	22,222	24,000	9%	9%	7%		
Crane machinery	31,006	35,657	39,222	33,221	38,204	41,260	7%	7%	5%		
Others	7,561	10,964	14,253	8,401	12,182	15,837	11%	11%	11%		
Agricultural machinery	1,836	2,020	2,222	2,058	2,367	2,651	12%	17%	19%		
Financial services	843	927	974	938	1,051	1,156	11%	13%	19%		
Total revenue	58,902	69,872	79,005	63,942	76,025	84,903	9%	9%	7%		
Revenue growth							Change in ppt				
Construction machinery	37.2%	19.0%	13.3%	48.7%	19.1%	11.7%	11.5	0.1	(1.6)		
Concrete machinery	27.0%	15.0%	10.0%	39.0%	15.0%	8.0%	12.0	0.0	(2.0)		
Crane machinery	40.0%	15.0%	10.0%	50.0%	15.0%	8.0%	10.0	0.0	(2.0)		
Others	53.0%	45.0%	30.0%	70.0%	45.0%	30.0%	17.0	0.0	0.0		
Agricultural machinery	16.0%	10.0%	10.0%	30.0%	15.0%	12.0%	14.0	5.0	2.0		
Financial services	15.0%	10.0%	5.0%	28.0%	12.0%	10.0%	13.0	2.0	5.0		
Total revenue growth	36.0%	18.6%	13.1%	47.6%	18.9%	11.7%	11.6	0.3	(1.4)		
Gross margin							Change in ppt				
Construction machinery	29.7%	30.2%	30.2%	28.3%	28.7%	28.7%	-1.50	-1.49	-1.48		
Concrete machinery	27.8%	28.5%	28.5%	27.4%	27.5%	27.5%	-0.40	-1.00	-1.00		
Crane machinery	32.5%	33.0%	33.0%	30.2%	31.0%	31.0%	-2.30	-2.00	-2.00		
Others	23.0%	24.0%	25.0%	22.5%	23.5%	24.5%	-0.50	-0.50	-0.50		
Agricultural machinery	8.0%	10.0%	11.0%	9.0%	12.0%	13.0%	1.00	2.00	2.00		
Financial services	99.5%	100.0%	100.0%	99.5%	100.0%	100.0%	0.00	0.00	0.00		
Average gross margin	30.1%	30.5%	30.5%	28.7%	29.1%	29.2%	-1.39	-1.37	-1.32		
Net profit	7,206	8,933	10,175	6,887	8,727	9,928	-4%	-2%	-2%		

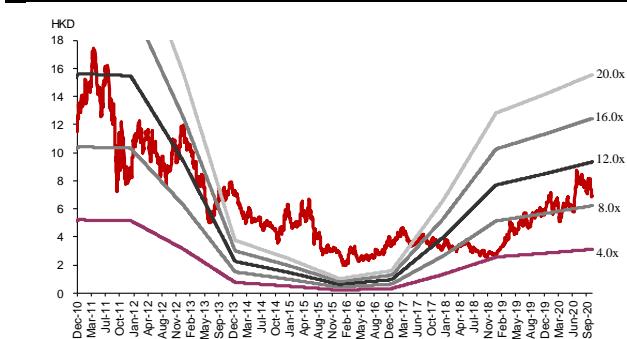
Source: Company data, CMBIS estimates

Figure 3: Zoomlion's revenue trend

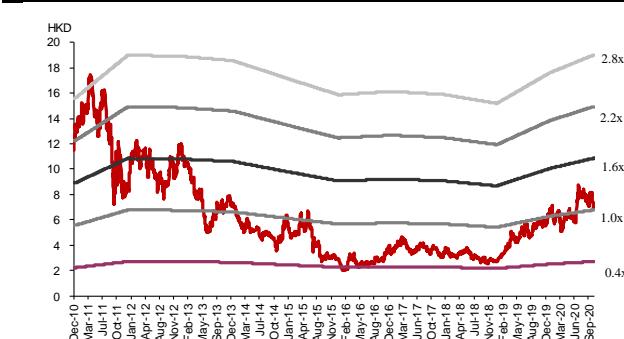
Source: Company data, CMBIS estimates

Figure 4: Zoomlion's gross margin trend

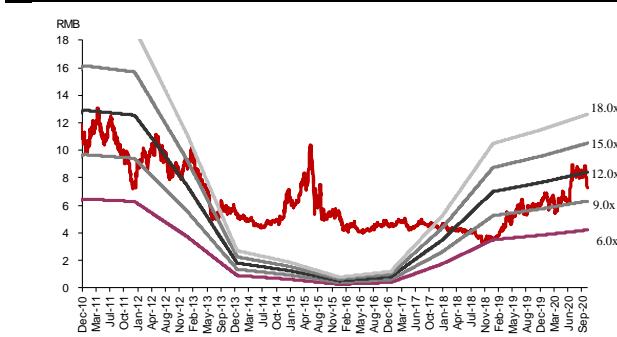
Source: Company data, CMBIS estimates

Figure 5: Zoomlion - H 12M forward P/E band

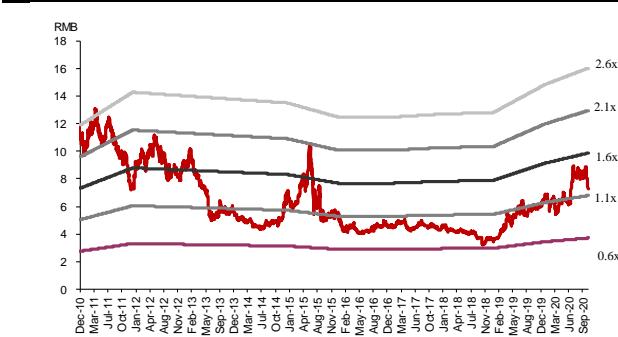
Source: Bloomberg, Company data, CMBIS estimates

Figure 6: Zoomlion – H 12M forward P/B band

Source: Bloomberg, Company data, CMBIS estimates

Figure 7: Zoomlion - A 12M forward P/E band

Source: Bloomberg, Company data, CMBIS estimates

Figure 8: Zoomlion – A 12M forward P/B band

Source: Bloomberg, Company data, CMBIS estimates

- **Risk factors:** (1) Unexpected weakness on infrastructure spending; (2) Slow recovery of property construction; (3) Risks of new business expansion.

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue	28,697	43,307	63,942	76,025	84,903
Cost of sales	-20,923	-30,314	-45,605	-53,874	-60,132
Gross profit	7,774	12,993	18,336	22,152	24,771
Other income	882	1,017	1,048	978	978
S&D expenses	-2,379	-3,780	-4,604	-5,322	-5,858
Administrative expenses	-2,063	-2,693	-3,709	-4,333	-4,839
R&D expenses	-581	-1,516	-2,877	-3,421	-3,821
EBIT	3,633	6,021	8,194	10,054	11,231
Net finance income/(cost)	-1,205	-1,165	-519	-278	-90
Finance income	347	539	575	793	875
Finance expenses	-1,552	-1,704	-1,094	-1,071	-964
Other gains/(losses)	0	0	0	0	0
Profit of JV and associates	222	188	254	271	288
Pretax profit	2,650	5,044	7,929	10,047	11,430
Income tax	-682	-759	-1,110	-1,407	-1,600
After tax profit	1,968	4,285	6,819	8,640	9,830
MI/discontinued operation	63	96	68	86	98
Net profit	2,031	4,381	6,887	8,727	9,928
D&A	837	817	923	1,005	1,080
EBITDA	4,470	6,838	9,117	11,059	12,311

Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Pretax profit	2,650	5,044	7,929	10,047	11,430
Finance cost	1,451	1,704	1,094	1,071	964
Interest income	-347	-539	-575	-793	-875
Profit or loss of associates	-222	-188	-254	-271	-288
Disposal of PP&E/business	-152	0	0	0	0
Depreciation and amortization	837	817	923	1,005	1,080
Income tax paid	-431	-773	-1,110	-1,407	-1,600
Change in working capital	1,152	442	-2,404	-3,816	-4,238
Others	-221	-539	0	0	0
Cash flow from operation	4,717	5,968	5,603	5,837	6,473
Net capex on PP&E	-272	-1,082	-2,246	-2,646	-2,500
Investment in JV/associates	-4	-301	0	0	0
Investment in subsidiaries	0	-177	0	0	0
Investment in intangible assets	-103	-128	-100	0	0
Dividend received	4	45	0	0	0
Interest received	347	253	575	793	875
Others	-7,214	11,374	0	0	0
Cash flow from investing	-7,242	9,984	-1,771	-1,853	-1,625
Equity financing/(repurchase)	37	-2,145	0	6,906	0
Net bank borrowings	6,817	-14,008	-1,000	100	-4,100
Dividend paid	-1,308	-1,801	0	-2,941	-3,491
Interest paid	-1,428	-1,707	-1,094	-1,071	-964
Others	-16	13	0	0	0
Cash flow from financing	4,102	-19,648	-2,094	2,995	-8,555
Change in cash	1,577	-3,696	1,738	6,978	-3,707
Cash at beginning of the year	7,148	8,754	5,073	6,811	13,789
Exchange and others	29	15	0	0	0
Cash at the end of the year	8,754	5,073	6,811	13,789	10,082

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	28,657	37,979	43,810	46,636	51,975
PP&E	6,077	6,735	8,324	10,234	11,922
Lease prepayment	1,943	2,433	2,383	2,333	2,283
JV/associates	3,500	3,909	4,163	4,434	4,723
Finance lease receivables	3,656	7,771	9,047	10,116	10,354
Goodwill	2,046	2,017	2,017	2,017	2,017
Trade receivables	5,498	9,072	11,950	11,795	15,188
Intangible assets	2,153	2,043	1,927	1,708	1,489
Financial assets	2,379	2,644	2,644	2,644	2,644
Others	0	0	0	0	0
Deferred tax assets	1,276	1,271	1,271	1,271	1,271
Deposits	129	84	84	84	84
Current assets	64,762	54,052	70,624	75,370	86,854
Inventories	9,551	11,772	14,217	14,417	17,543
Trade & other receivables	21,554	20,839	25,409	28,329	33,080
Finance lease receivables	8,835	9,229	17,048	11,695	19,009
Financial assets at FVPL	13,787	4,311	4,311	4,311	4,311
Others	1,097	1,413	1,413	1,413	1,413
Pledged deposits	1,184	1,415	1,415	1,415	1,415
Cash	8,754	5,073	6,811	13,789	10,082
Current liabilities	39,623	34,569	50,953	45,919	60,603
Trade and other payables	15,786	25,012	41,210	35,542	50,126
Bank borrowings	22,044	7,312	7,112	7,212	7,312
Tax payable	151	186	186	186	186
Contract liabilities	1,602	1,934	2,321	2,855	2,855
Others	40	125	125	125	125
Non-current liabilities	15,065	17,965	17,165	17,165	12,965
Bank borrowings	13,645	14,515	13,715	13,715	9,515
Deferred tax liabilities	429	455	455	455	455
Others	991	2,995	2,995	2,995	2,995
Equity	38,731	39,497	46,316	58,922	65,261
Shareholders' equity	38,164	38,827	45,714	58,406	64,844
MI	567	670	602	515	417

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Concrete machinery	35%	32%	30%	29%	28%
Crane machinery	43%	51%	52%	50%	49%
Others machinery	14%	11%	13%	16%	19%
Agricultural machinery	5%	4%	3%	3%	3%
Financial services	2%	2%	1%	1%	1%
Environmental (discontinued)	0%	0%	0%	0%	0%
Total	100%	100%	100%	100%	100%
Profit & loss ratio (%)					
Gross margin	27.1	30.0	28.7	29.1	29.2
EBIT margin	12.7	13.9	12.8	13.2	13.2
Net profit margin	6.9	9.9	10.7	11.4	11.6
Growth (%)					
Revenue	39.3	50.9	47.6	18.9	11.7
Gross profit	80.6	67.1	41.1	20.8	11.8
EBIT	n/a	65.7	36.1	22.7	11.7
Net profit	51.3	115.7	57.2	26.7	13.8
Balance sheet ratio					
Current ratio (x)	1.6	1.6	1.4	1.6	1.4
Trade receivable turnover days	342	240	192	186	190
Finance lease receivable turnover days	161	124	123	115	110
Inventory turnover days	161	128	104	97	97
Payable turnover days	268	246	265	260	260
Net debt / total equity (%)	33.6	31.3	20.8	4.7	3.6
Profitability (%)					
ROA	2.3	4.7	6.7	7.4	7.6
ROE	5.4	11.4	16.3	16.8	16.1
Per share data					
EPS (RMB)	0.27	0.58	0.87	0.96	1.09
BVPS (RMB)	4.89	4.93	5.80	6.40	7.10
DPS (RMB)	0.25	0.00	0.37	0.38	0.44

Note: We have modelled the dilution effect from upcoming fund raising exercise in 2021E

Source: Company data, CMBIS estimates

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.

CMBIS 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 CMBIS
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 Securities Limited

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

CMB International Securities Limited ("CMBIS") 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. CMBIS 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. CMBIS 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 CMBIS, solely for the purpose of supplying information to the clients of CMBIS 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 CMBIS 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. CMBIS has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIS provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIS 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. CMBIS may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIS 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 CMBIS 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 CMBIS may have a conflict of interest that could affect the objectivity of this report and CMBIS 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 CMBIS.

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 CMBIS.

For recipients of this document in the United States

CMBIS is not a registered broker-dealer in the United States. As a result, CMBIS 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.