

Jiangsu Hengli Hydraulic (601100 CH)

Net profit in 2Q21 down only 2% YoY; slightly better than expectations

Despite the fact that industry demand for excavator was weak and steel cost was high in 2Q21, Hengli's net profit in 2Q21 only dropped 2% YoY to RMB626mn which is slightly better than expectation. Net profit in 1H21 grew 43% YoY to RMB1.41bn, which accounted for 48% of our full year estimates (run rate in 1H20: 43%). It's worth noting that the revenue from pump, valve and other products exceeded that of the excavator hydraulic cylinder in 1H21, a key driver for the resilient results. We expect Hengli's production volume of hydraulic cylinders in Aug to see >10% YoY growth, and expect an acceleration in 4Q21E on the back of better infrastructure spending growth. That said, we maintain our **HOLD** rating as we believe the stock is fairly-priced at 43x 2021E P/E. We maintain our TP of RMB103 (based on unchanged 46x 2021E P/E).

- Key financials in 1H21.** Revenue in 1H21 grew 51% YoY to RMB5.2bn. Gross margin held up well at 41% (down only 0.9ppt YoY). Operating cash inflow grew 25% YoY to RMB1.19bn, which is healthy in our view. In 2Q21, Hengli managed to deliver 14% YoY revenue growth while gross margin remained stable at 41% QoQ despite the high steel cost.
- Hydraulic cylinder better than our expectation.** Sales volume of hydraulic cylinder (for excavator) grew 44% YoY to 474k units in 1H21. The sales volume growth outpaced the excavator industry sales volume growth of 38%. ASP slightly dropped 4% YoY to RMB4,177 / unit. Sales volume of non-standardized cylinders grew 23% YoY to 78.8k units in 1H21 and ASP increased 19% YoY to RMB10.7k/unit due to product mix improvement in our view.
- Explosive growth of pump, valve and motor continued.** Revenue from Hengli Hydraulic Technology (major products include pump, valve and motor) surged 78% YoY to RMB2.1bn in 1H21, which exceeded the revenue from excavator hydraulic cylinder (RMB1.98bn).
- Upside risks:** (1) Strong market share gain; (2) better-than-expected excavator demand. **Downside risks:** (1) Continuous slowdown of construction activities; (2) risk of overseas expansion.

Earnings Summary

(YE 31 Dec)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue (RMB mn)	5,414	7,855	10,063	10,936	11,567
YoY growth (%)	28.6	45.1	28.1	8.7	5.8
Net income (RMB mn)	1,296	2,254	2,932	3,307	3,713
EPS (RMB)	0.99	1.73	2.25	2.53	2.84
YoY growth (%)	54.9	73.9	30.1	12.8	12.3
Consensus EPS (RMB)	NA	NA	2.28	2.75	3.19
EV/EBITDA (x)	74.4	41.2	35.5	32.5	29.9
P/E (x)	96.6	55.6	42.7	37.9	33.7
P/B (x)	22.4	17.1	13.2	10.7	8.8
Yield (%)	0.4	0.6	0.8	0.9	1.0
ROE (%)	25.6	35.0	35.0	31.2	28.5
Net debt / equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIS estimates

HOLD (Maintain)

Target Price: RMB103.00
(Previous TP) RMB103.00
Up/Downside: +7%
Current Price: RMB95.97

China Capital Goods

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Stock Data

Mkt Cap (RMB mn)	125,275
Avg 3 mths t/o (RMB mn)	969
52w High/Low (RMB)	137.66/60.56
Total Issued Shares (mn)	1,305

Source: Bloomberg

Shareholding Structure

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

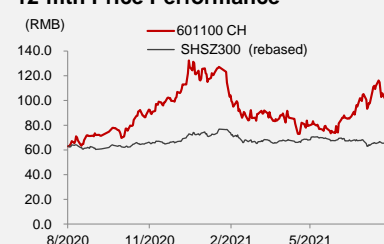
Source: Company data

Share Performance

	Absolute	Relative
1-mth	-10.4%	-3.2%
3-mth	18.0%	27.0%
6-mth	-9.2%	6.6%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: RSM

- Construction Machinery / HDT (Outperform) – Favourable policy shift; Defensive growth amid volatile market; Upgrade SANY Heavy & Sinotruk – 9 Aug 2021
- Construction Machinery / HDT (Market Perform) – Approaching the peak of upcycle; D/G Hengli, SANY Heavy & Sinotruk – 26 May 2021
- Jiangsu Hengli – Earnings impressive but we are now more conservative on valuation – 27 Apr 2021

Figure 1: 1H21 results highlights

YE Dec 31(RMB mn)	1H20	1H21	Change (YoY)
Total revenue	3,456	5,227	51.2%
Cost of sales	-2,009	-3,083	53.4%
Gross profit	1,446	2,144	48.2%
Surcharge	-36	-46	28.2%
S&D expenses	-55	-46	-16.9%
Administrative expenses	-205	-356	73.2%
Asset impairment	-43	-11	-73.4%
EBIT	1,107	1,685	52.2%
Net finance income/(cost)	34	-41	n/a
Finance income	97	99	1.6%
Finance expenses	-63	-140	122.2%
Other gains/(losses)	36	37	3.9%
Share of profit of JV and associates	0	0	n/a
Pretax profit	1,177	1,681	42.8%
Income tax	-189	-269	42.6%
After tax profit	988	1,412	42.9%
MI	-2	-3	38.4%
Net profit	986	1,409	42.9%
D&A	138	221	60.0%
EBITDA	1,245	1,906	53.1%

Source: Company data, CMBIS

Figure 2: 2Q21 results highlights

(RMB mn)	1Q20	1Q21	Change YoY	2Q20	2Q21	Change YoY
Total revenue	1,369	2,857	108.7%	2,087	2,370	13.6%
Cost of sales	-850	-1,684	98.1%	-1,159	-1,398	20.6%
Gross profit	518	1,172	126.2%	928	972	4.7%
Other income	-13	-30	121.6%	-23	-17	-27.0%
S&D expenses	-26	-30	12.2%	-29	-16	-43.6%
Administrative expenses	-97	-168	72.8%	-108	-188	73.6%
Asset impairment	-18	-23	22.7%	-24	11	-146.1%
EBIT	363	922	154.2%	744	763	2.5%
Net finance income/(cost)	37	-2	n/a	-3	-39	1183.9%
Other gains/(loss)	18	18	-2.7%	18	20	10.7%
Profit of JV & associates	0	0	n/a	0	0	n/a
Pretax profit	418	937	124.2%	759	744	-2.0%
Income tax	-70	-153	118.0%	-118	-116	-2.2%
After tax profit	348	784	125.4%	641	628	-2.0%
MI	-1	-1	77.4%	-2	-2	24.7%
Net profit	347	783	125.5%	639	626	-2.0%
Key ratios			<i>ppt</i>			<i>ppt</i>
Gross margin	37.9%	41.0%	3.2	44.5%	41.0%	-3.5
S&D expense ratio	1.9%	1.0%	-0.9	1.4%	0.7%	-0.7
Administrative and R&D exp ratio	7.1%	5.9%	-1.2	5.2%	7.9%	2.7
Effective tax rate	16.8%	16.4%	-0.5	15.6%	15.6%	-0.0

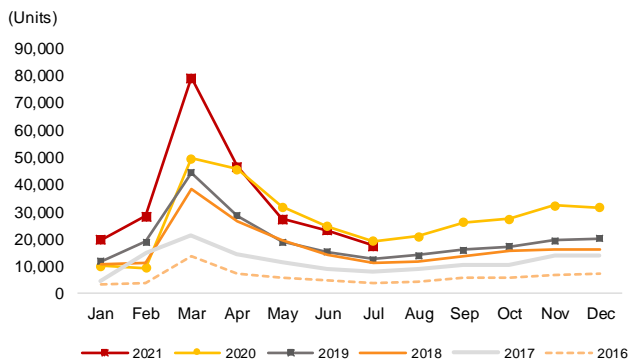
Source: Company data, CMBIS

Figure 3: Key assumptions

(RMB mn)	2019	2020	2021E	2022E	2023E
Revenue					
Hydraulic cylinder for excavator	2,188	3,127	3,645	3,645	3,645
Specialised hydraulic cylinder for heavy equipment	1,353	1,370	1,563	1,720	1,771
Hydraulic pump and valve	1,161	2,338	3,624	4,168	4,585
Completed set of equipment	189	157	196	216	237
Component	501	845	1,015	1,167	1,307
Revenue (hydraulic business)	5,392	7,838	10,044	10,916	11,546
Other business	22	17	19	21	22
Total revenue	5,414	7,855	10,063	10,936	11,567
Revenue growth					
Hydraulic cylinder for excavator	20.8%	43.0%	16.6%	0.0%	0.0%
Specialised hydraulic cylinder for heavy equipment	18.3%	1.3%	14.1%	10.0%	3.0%
Hydraulic pump and valve	142.6%	101.3%	55.0%	15.0%	10.0%
Completed set of equipment	-5.9%	-16.9%	25.0%	10.0%	10.0%
Component	-6.8%	68.8%	20.0%	15.0%	12.0%
Revenue (hydraulic business)	29.2%	45.4%	28.1%	8.7%	5.8%
Other business	-43.2%	-23.1%	10.0%	10.0%	5.0%
Total revenue	28.6%	45.1%	59.2%	8.7%	5.8%
Gross margin					
Hydraulic cylinder for excavator	42.1%	46.8%	41.0%	41.0%	41.0%
Specialised hydraulic cylinder for heavy equipment	35.1%	46.8%	39.0%	39.0%	39.0%
Hydraulic pump and valve	37.8%	52.3%	44.0%	43.0%	43.0%
Completed set of equipment	29.1%	45.7%	35.0%	35.0%	34.0%
Component	27.9%	6.2%	20.0%	25.0%	33.0%
Gross margin (hydraulic business)	37.6%	44.0%	39.5%	39.6%	40.4%
Other business	66.3%	74.3%	66.0%	66.0%	66.0%
Average gross margin	37.8%	44.1%	39.6%	39.7%	40.5%

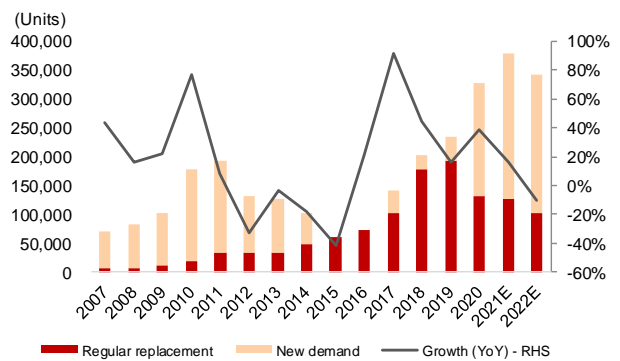
Source: Company data, CMBIS estimates

Figure 4: Excavator monthly sales volume (industry)



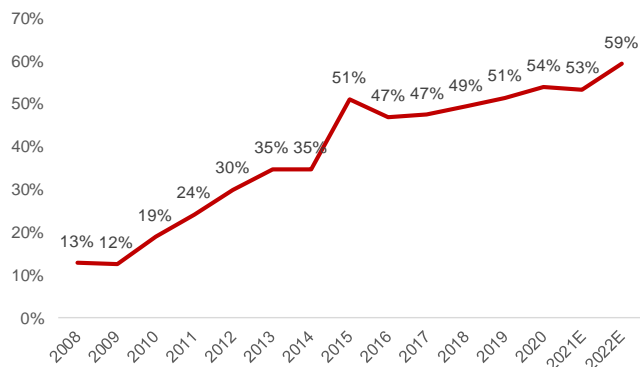
Note: Estimated figure for Apr 2021
 Source: CCMA, CMBIS estimates

Figure 5: CMBIS excavator sales projection (industry)



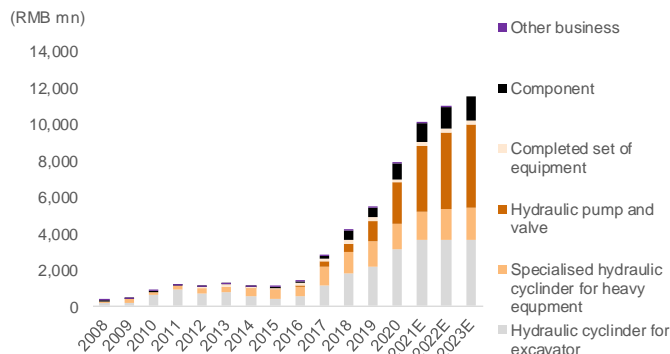
Source: Company data, CMBIS estimates

Figure 6: Hengli's market share in hydraulic cylinder for excavator



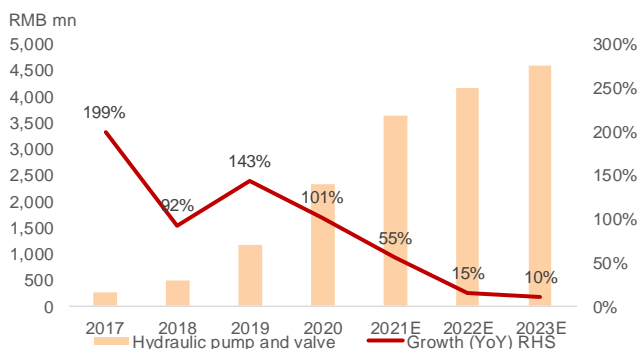
Source: Company data, CMBIS estimates

Figure 7: Hengli's revenue breakdown



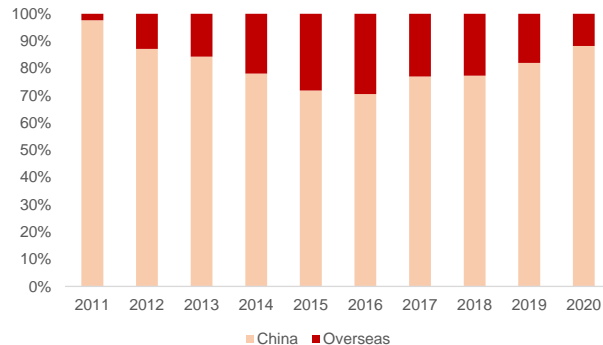
Source: Company data, CMBIS estimates

Figure 8: Hengli's revenue of pump & valves



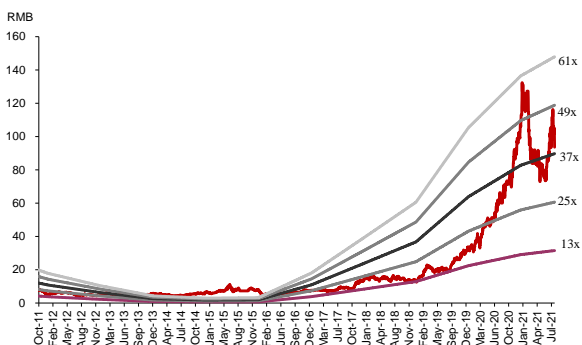
Source: Company data, CMBIS estimates

Figure 9: Revenue breakdown by region



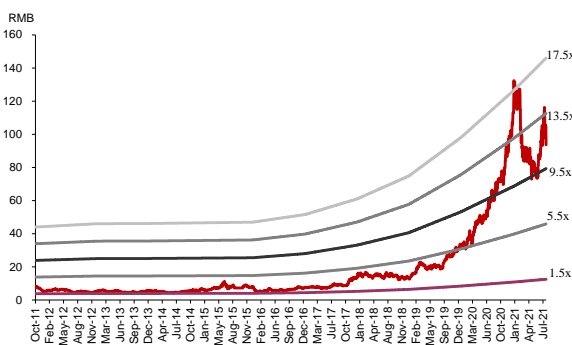
Source: Company data, CMBIS

Figure 10: Hengli's P/E band



Source: Bloomberg, Company data, CMBIS estimates

Figure 11: Hengli's P/B band



Source: Bloomberg, Company data, CMBIS estimates

Financial Summary

Income statement						Cash flow summary					
YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E	YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	5,414	7,855	10,063	10,936	11,567	Pretax profit	1,493	2,609	3,456	3,899	4,377
Cost of sales	-3,369	-4,391	-6,080	-6,598	-6,884	Finance cost	-33	146	43	39	39
Gross profit	2,045	3,464	3,983	4,338	4,683	Profit or loss of associates	0	0	0	0	0
Surcharge	-52	-72	-101	-109	-116	Loss/(gain) on disposal	1	1	0	0	0
S&D expenses	-111	-107	-121	-131	-139	Depreciation & amortization	264	311	338	369	394
Administrative expenses	-435	-509	-624	-667	-694	Income tax paid	-375	-714	-518	-585	-657
Asset impairment	-52	-90	0	0	0	Change in working capital	66	-849	-442	148	-343
EBIT	1,395	2,687	3,138	3,431	3,735	Others	253	488	0	0	0
Net finance income/(cost)	31	-151	218	359	527	Cash flow from operation	1,660	1,981	2,877	3,869	3,810
Finance income	187	223	260	398	565	Net capex on PP&E	-434	-380	-500	-500	-400
Finance expenses	-156	-375	-43	-39	-39	Investment in JV/associates	0	0	0	0	0
Other gains/(losses)	67	74	101	109	116	Investment in subsidiaries	0	0	0	0	0
Profit of JV and associates	0	0	0	0	0	Investment in intangibles	-4	-19	-20	-20	-20
Pretax profit	1,493	2,609	3,456	3,899	4,377	Dividend received	0	0	0	0	0
Income tax	-195	-348	-518	-585	-657	Others	-14	-264	0	0	0
After tax profit	1,298	2,261	2,938	3,314	3,720	Cash flow from investing	-452	-663	-520	-520	-420
MI	-2	-7	-6	-7	-7	Equity financing/(repurchase)	0	0	0	0	0
Net profit	1,296	2,254	2,932	3,307	3,713	Net bank borrowings	-100	-361	-150	0	0
						Dividend paid	-265	-529	-783	-1,026	-1,158
D&A	264	311	338	369	394	Interest paid	-107	-40	-43	-39	-39
EBITDA	1,659	2,997	3,476	3,800	4,128	Others	18	112	0	0	0
						Cash flow from financing	-454	-818	-976	-1,065	-1,196
						Change in cash	754	499	1,381	2,285	2,194
						Cash at beginning of the year	1,571	2,343	2,777	4,158	6,443
						Exchange and others	18	-66	-0	-0	-0
						Cash at the end of the year	2,343	2,777	4,158	6,443	8,636

Balance sheet						Key ratios					
YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E	YE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Non-current assets	2,935	3,025	3,207	3,358	3,384	Sales mix (%)					
PP&E	2,364	2,432	2,608	2,753	2,774	Cylinder for excavator	40%	40%	36%	33%	32%
JV/associates	0	0	0	0	0	Cylinder for heavy equipment	25%	17%	16%	16%	15%
Goodwill	0	0	0	0	0	Hydraulic pump and valve	21%	30%	36%	38%	40%
Intangible assets	273	280	286	292	297	Hydraulic system	3%	2%	2%	2%	2%
AFS investments	0	0	0	0	0	Component	9%	11%	10%	11%	11%
Others	257	261	261	261	261	Other business	0%	0%	0%	0%	0%
Deferred tax assets	41	52	52	52	52	Total revenue	100%	100%	100%	100%	100%
Current assets	5,492	7,595	9,821	11,854	14,624	Profit & loss ratio (%)					
Inventories	997	1,217	1,848	1,442	1,953	Gross margin	37.8	44.1	39.6	39.7	40.5
Trade and bill receivables	1,639	2,705	2,919	3,073	3,138	EBIT margin	25.8	34.2	31.2	31.4	32.3
Prepayment	98	164	164	164	164	Net profit margin	24.0	28.8	29.2	30.3	32.2
Others	414	733	733	733	733	Growth (%)					
Pledged deposits	0	0	0	0	0	Revenue	28.6	45.1	28.1	8.7	5.8
Cash	2,343	2,777	4,158	6,443	8,636	Gross profit	32.7	69.4	15.0	8.9	7.9
Current liabilities	2,170	2,590	2,894	2,789	3,022	EBIT	58.7	92.7	16.8	9.3	8.9
Trade and bill payables	791	1,131	1,534	1,430	1,663	Net profit	54.9	73.9	30.1	12.8	12.3
Bank borrowings	937	554	454	454	454	Balance sheet ratio					
Tax payable	62	119	119	119	119	Current ratio (x)	2.5	2.9	3.4	4.2	4.8
Advance from customers	192	108	108	108	108	Receivable turnover days	100	101	102	100	98
Others	188	677	677	677	677	Inventory turnover days	111	92	92	91	90
Non-current liabilities	643	679	629	629	629	Payable turnover days	80	80	80	82	82
Bank borrowings	200	370	320	320	320	Net debt / total equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Deferred tax liabilities	70	108	108	108	108	Profitability (%)					
Deferred income	223	200	200	200	200	ROA	16.5	23.7	24.8	23.4	22.4
Others	150	0	0	0	0	ROE	25.6	35.0	35.0	31.2	28.5
Equity	5,614	7,352	9,506	11,794	14,357	Per share data					
Shareholders' equity	5,584	7,314	9,462	11,743	14,299	EPS (RMB)	0.99	1.73	2.25	2.53	2.84
MI	30	38	44	50	58	BVPS (RMB)	4.28	5.60	7.25	9.00	10.95
						DPS (RMB)	0.41	0.60	0.79	0.89	1.00

Source: Company data, CMBIS estimates

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