

ZTE (763 HK)

Strong 1Q22 results; continuing improvement in operation and business development

ZTE announced 1Q22 results. 1Q22's revenue/NP to shareholders grew 6.4%/1.6% YoY to RMB27.9bn/RMB2.2bn, respectively. We think the results are solid and largely in-line with our expectations. Looking forward, we remain positive on ZTE's business development and continuing improvement of operation. Maintain BUY, with unchanged TP of HK\$29.65.

- 1Q22 results in line with expectations.** 1Q22 revenue/NP to shareholders accounted for 22%/28% of our full year forecasts. 1Q22's GPM increased to 37.8% vs. 35.2% in FY21, led by higher GPM from telecom segment. NP before extraordinary items grew 117% YoY, suggesting an improvement of business operations. Looking forward, we expect FY22E revenue to grow at 12.9% YoY, while NP to shareholders to grow at 15.7% YoY.
- Telco's FY22E capex to grow 4% YoY and ZTE to gain share.** China telecom operators announced FY22E capex budget, a total of RMB352bn (4% YoY increase). The pace of 5G BTS deployment are steady, with 670k 5G BTS planned for 2022 (vs. 640k/650k for 2020/21). However, 5G-related capex budget reduced slightly by 5%, due to BTS de-spec trend as the growth momentum for 5G investment is easing. We maintain our positive outlook for ZTE and believe its carrier revenue growth should exceed the telco's capex growth (6.1% vs. 3.9%). The Company will still be a key beneficiary as the telco is shifting its investment from 5G infrastructure to industrial digitalization. Currently, ZTE's share in telco's capex is ~22.3%, which we expect to rise slightly to 22.8% in 2022.
- Maintain BUY with TP unchanged at HK\$29.65.** Current valuation is attractive after significant broad market pullback as investors have concerns on 1) China lockdown resulting in a weaker than expected economy; 2) Russian/Ukraine conflict is driving higher material costs; 3) lingered supply constraints and worldwide inflation. Potential risks include Sino-U.S. trade tension, additional component restriction/technology ban, and 5G deployment delays.

Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Turnover (RMB mn)	101,451	114,522	129,803	146,400	163,351
YoY growth (%)	11.8%	12.9%	13.3%	12.8%	11.6%
Gross margin (%)	31.6%	35.2%	35.6%	35.2%	35.0%
Net profit (RMB mn)	4,260	6,813	7,845	9,096	10,253
YoY growth (%)	-17.3%	59.9%	15.1%	15.9%	12.7%
Diluted EPS (RMB)	0.92	1.47	1.66	1.92	2.17
YoY growth (%)	-24.8%	59.8%	12.8%	15.9%	12.7%
Consensus EPS (RMB)	NA	NA	1.72	1.98	2.11
PE (x)	13.7	8.6	7.6	6.6	5.8
Yield (%)	1.1%	1.1%	1.1%	1.1%	1.1%
ROE (%)	9.8%	13.2%	13.4%	13.7%	13.5%
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	HK\$29.65
(Previous TP)	HK\$29.65)
Up/Downside	+91.6%
Current Price	HK\$15.48

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Stock Data

Mkt. Cap. (HK\$ mn)	115,517
Avg. 3mths t/o (HK\$ mn)	136
52W High/Low (HK\$)	31.75/12.7
Total Issued Shares (mn)	755.5

Source: Bloomberg

Shareholding Structure

BlackRock	8.58%
Capital Group	5.08%
Schroders	4.93%

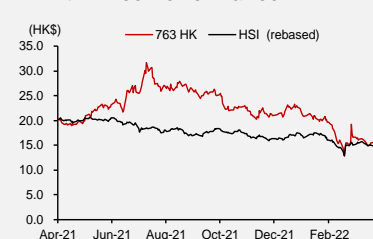
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	-7.0%	-1.1%
3-mth	-27.9%	-13.9%
6-mth	-35.2%	-17.9%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Ernst & Young

Related Reports

- ZTE (763 HK) – Overhang removed; Focus on core business development – 24 Mar 2022
- ZTE (763HK) – ZTE finished 2021 with good results; Positive potentials could materialize ahead – 31 Jan 2022

Figure 1: Earnings revision

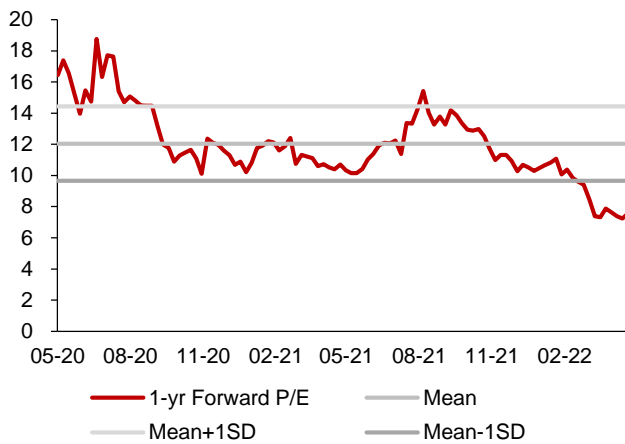
US\$ mn	New			Old			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	129,803	146,400	163,351	129,803	146,400	na	0%	0%	na
Gross Profit	46,196	51,526	57,112	45,693	51,515	na	2%	1%	na
Operating Profit	9,740	11,286	12,719	10,192	11,713	na	0%	-1%	na
Net profit	7,845	9,096	10,253	7,806	8,975	na	0%	-1%	na
EPS (US\$ cents)	1.66	1.92	2.17	1.64	1.85	na	0%	-1%	na
Gross Margin	35.6%	35.2%	35.0%	35.2%	35.2%	na	0.5 ppt	0.2 ppt	na
Operating Margin	7.5%	7.7%	7.8%	7.9%	8.0%	na	0 ppt	-0.1 ppt	na
Net Margin	6.0%	6.2%	6.3%	6.0%	6.1%	na	0 ppt	-0.1 ppt	na

Source: Company data, CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

US\$ mn	CMBIGM			Consensus			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	129,803	146,400	163,351	129,849	144,251	154,494	0%	1%	6%
Gross Profit	46,196	51,526	57,112	45,797	50,620	54,405	1%	2%	5%
Operating Profit	9,740	11,286	12,719	9,561	10,984	11,472	2%	3%	11%
Net profit	7,845	9,096	10,253	8,050	9,260	9,926	-3%	-2%	3%
EPS (US\$ cents)	1.66	1.92	2.17	1.72	1.98	2.11	-4%	-3%	3%
Gross Margin	35.6%	35.2%	35.0%	35.3%	35.1%	35.2%	0.3 ppt	0.1 ppt	-0.3 ppt
Operating Margin	7.5%	7.7%	7.8%	7.4%	7.6%	7.4%	0.1 ppt	0.1 ppt	0.4 ppt
Net Margin	6.0%	6.2%	6.3%	6.2%	6.4%	6.4%	-0.2 ppt	-0.2 ppt	-0.1 ppt

Source: Company data, CMBIGM estimates

Figure 3: 12M forward P/E chart

Source: Company data, CMBIGM estimates

Figure 4: 12M forward P/E band

Source: Company data, CMBIGM estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	101,451	114,522	129,803	146,400	163,351
Cost of sales	(69,379)	(74,160)	(83,607)	(94,875)	(106,239)
Gross profit	32,071	40,362	46,196	51,526	57,112
Selling exp	(7,579)	(8,733)	(9,898)	(11,164)	(12,457)
Admin exp	(4,995)	(5,445)	(5,929)	(6,541)	(7,134)
R&D exp	(14,797)	(18,804)	(21,313)	(23,424)	(26,136)
Finance costs	(421)	(963)	212	473	814
Other operating exp.	1,191	2,259	472	416	520
Operating profit	5,471	8,676	9,740	11,286	12,719
Other non-oper exp.	(407)	(177)	(225)	(254)	(284)
Pre-tax profit	5,064	8,499	9,515	11,032	12,435
Income tax expense	(342)	(1,463)	(1,427)	(1,655)	(1,865)
Minority interests	(446)	(223)	(243)	(281)	(317)
Net profit to shareholders	4,260	6,813	7,845	9,096	10,253

Cash flow summary

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Net profit	4,722	7,036	8,087	9,377	10,570
Depreciation/amortization	1,465	1,671	1,687	1,723	1,777
Change in working capital	(1,965)	2,615	(2,364)	(6,318)	(3,939)
Others	6,011	4,401	6,434	7,411	7,776
Net cash from operating	10,233	15,724	13,844	12,193	16,185
Capex	(6,472)	(5,686)	(3,993)	(4,476)	(4,902)
Other	(610)	(4,906)	(1,430)	1,110	1,218
Net cash from investing	(7,082)	(10,592)	(5,423)	(3,366)	(3,684)
Share issuance	14,167	538	0	0	0
Dividend paid	(2,951)	(2,618)	(2,531)	(2,726)	(2,974)
Other	(11,505)	4,859	2,474	6,284	6,141
Net cash from financing	(290)	2,779	(57)	3,559	3,167
Net change in cash	2,861	7,910	8,365	12,386	15,667
Cash at beginning of the year	28,506	31,403	39,071	47,436	59,821
Exchange difference	37	(242)	0	0	0
Cash at the end of the year	31,403	39,071	47,436	59,821	75,488

Balance sheet

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Current assets	106,977	127,871	140,763	162,262	179,434
Cash & equivalents	35,660	50,713	62,173	74,559	90,226
Account receivables	15,891	17,509	18,053	20,452	20,722
Inventory	33,689	36,317	36,983	40,996	40,502
Prepayment	322	607	495	576	633
Other current assets	21,415	22,725	23,058	25,679	27,353
Non-current assets	43,658	40,892	38,889	38,456	38,252
PPE	11,914	11,437	11,102	11,000	11,055
Deferred tax assets	3,437	3,195	3,023	3,377	3,663
Other non-current assets	28,307	26,261	24,764	24,079	23,534
Total assets	150,635	168,763	179,652	200,717	217,686
Current liabilities	74,395	78,685	79,183	85,989	87,788
ST borrowings	10,559	8,947	8,701	10,024	11,317
Account payables	14,998	16,102	18,347	20,499	22,232
Tax payable	0	0	0	0	0
Other current liabilities	48,838	53,637	52,134	55,467	54,240
Non-current liabilities	30,117	36,791	40,021	45,849	51,395
LT borrowings	22,614	29,908	32,629	37,590	42,438
Deferred tax liability	134	150	161	180	195
Other non-current liabilities	7,369	6,732	7,231	8,079	8,762
Total liabilities	104,512	115,476	119,204	131,838	139,183
Share capital	4,613	4,731	4,731	4,731	4,731
Reserve	23,276	25,360	25,360	25,360	25,360
Retained earnings	14,824	20,651	27,502	35,573	44,791
Other	583	740	808	886	974
Minority interest	2,826	1,806	2,048	2,330	2,647
Total equity	46,123	53,288	60,448	68,879	78,503
Total liabilities and equity	150,635	168,763	179,652	200,717	217,686

Key ratios

YE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue mix					
Carrier business	74,018	75,712	80,327	85,338	90,343
Consumer business	16,160	25,731	32,497	39,989	47,986
Gov. and enterprise	11,272	13,079	16,979	21,073	25,022
Growth (%)					
Revenue	11.8%	12.9%	13.3%	12.8%	11.6%
Gross profit	-4.9%	25.8%	14.5%	11.5%	10.8%
Operating profit	-27.6%	58.6%	12.3%	15.9%	12.7%
Net profit	-17.3%	59.9%	15.1%	15.9%	12.7%
Profit & loss ratio (%)					
Gross margin	31.6%	35.2%	35.6%	35.2%	35.0%
Operating margin	5.4%	7.6%	7.5%	7.7%	7.8%
Net profit margin	4.2%	5.9%	6.0%	6.2%	6.3%
Balance sheet ratio					
Net debt/total equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Current ratio (x)	1.4	1.6	1.8	1.9	2.0
Receivable turnover days	64	53	50	48	46
Inventory turnover days	(161)	(172)	(160)	(150)	(140)
Payable turnover days	(93)	(96)	(90)	(75)	(60)
Profitability (%)					
ROE	9.8%	13.2%	13.4%	13.7%	13.5%
ROA	2.8%	4.0%	4.4%	4.5%	4.7%
Per share data (RMB)					
EPS	0.92	1.47	1.66	1.92	2.17
DPS	0.20	0.20	0.20	0.20	0.20
BPS	9.35	10.88	12.34	14.07	16.03

Source: Company data, CMBIGM estimates

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