

# Chinasoft International | 354 HK

Growing along with IT application innovation wave

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- ▶ **2H22 results a miss**
- ▶ **Making progress on new businesses**
- ▶ **Appealing valuation**

## Outperform (maintained)

Current price:

**HK\$5.11**

(mid-day close on 30 Mar 2023)

Target:

**HK\$7.10**

(down from HK\$8.23)

**2H22 results miss on top-line and margins.** Revenue slid 1% YoY to RMB10.0b in 2H22, versus 20% YoY growth in 1H22. The result was 14% below Bloomberg consensus. New business revenue grew 7% YoY to RMB3.4b, a sharp deceleration from 51% in 1H22. Blended GPM contracted 4.7ppt YoY/3.5ppt QoQ to 21.2%, dragged by Covid and fluctuating demand from major customers that led to higher one-time costs. In a tough environment, Chinasoft executed well on cost control that saw its opex-to-sales ratio inch down 2ppt YoY to 19%. Operating profit fell 58% YoY to RMB206m as OPM narrowed 2.9ppt YoY to 2.1%. Net profit plunged 70% YoY to RMB189m, missing consensus for RMB701m in the wake of revenue and GPM disappointments. For 2022, revenue grew 9% YoY to RMB20.0b as net profit fell 33% to RMB759m.

**Riding on IT application innovation.** Chinasoft has various project pipelines well positioned to capture the IT application innovation wave ("Xinchuang"). Leveraging the innovation capabilities of the OpenHarmony platform, the company has made progress developing a new universal IoT operating system that could be adopted by various industries. In the case of the cloud business, the company continues to extend its product matrix to cover a full range of digital transformation scenarios, from public cloud distribution to hybrid cloud solutions. Progress in the automotive industry, one of the company's strategic focuses, is well explained by its numerous benchmark projects at mainstream automakers such as FAW Group, Lotus, Jike, and Zhongqi Chuangzhi.

**Maintain Outperform.** We cut our 2023/2024F earnings forecast 16%/15% to reflect a 7%/7% revenue cut and lower gross margins. We cut our target price from HK\$8.23 to HK\$7.10, based on an unchanged 14x 2023F P/E. The stock is currently trading at 10x 2023 P/E or 8x 2024F P/E, a level we consider appealing against 40% EPS growth in 2022-2025F.

### Forecast and valuation

Year to 31 Dec	2021	2022	2023F	2024F	2025F
Revenue (RMB m)	18,398	20,005	25,507	30,608	35,199
YoY (%)	30.5	8.7	27.5	20.0	15.0
Net profit (RMB m)	1,137	759	1,317	1,666	2,035
YoY (%)	19.1	N/A	73.5	26.4	22.2
Fully diluted EPS (RMB)	0.38	0.25	0.44	0.55	0.67
YoY (%)	12.5	(34.4)	73.5	26.4	22.2
P/E (x)	11.1	17.6	10.1	7.7	6.4
DPS (HK\$)	0.03	0.03	0.04	0.05	0.06
Dividend yield (%)	0.6	0.6	0.8	1.0	1.2
P/B (x)	1.1	1.1	1.0	0.9	0.8
ROAE (%)	11.2	6.4	10.4	11.8	12.8
Net debt/equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash

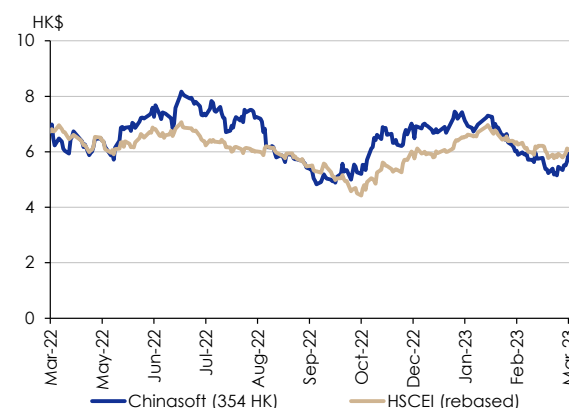
Source: Datastream Refinitive, CCBIS estimates

### Trading data

52-week range	HK\$8.44-4.72
Market capitalization (m)	HK\$15,410/US\$1,981
Shares outstanding (m)	3,016
Free float (%)	87
3M average daily T/O (m share)	12.6
3M average daily T/O (US\$ m)	11.9
Expected 12-month return (%)	39.0

Source: Datastream Refinitive, CCBIS estimates

### Share price vs HSCEI (rebased)



Source: Datastream Refinitive

### Stock performance

Performance over	1M	3M	12M
Absolute	(9)	(25)	(24)
Relative (%) to HSCEI	0	(27)	(15)

Source: Datastream Refinitive

## Chinasoft – 2H22/2022 results at a glance

RMB m	1H21	2H21	1H22	YoY (%/pp)	2H22	YoY (%/pp)	2021	2022	YoY (%/pp)
<b>Total revenue</b>	<b>8,341</b>	<b>10,057</b>	<b>10,025</b>	<b>20</b>	<b>(1)</b>	<b>8,341</b>	<b>18,398</b>	<b>20,005</b>	<b>9</b>
Gross profit	2,294	2,610	2,482	8	(19)	2,294	4,904	4,600	(6)
GPM (%)	27.5	26.0	24.8	(2.7)	(4.7)	27.5	26.7	23.0	(3.7)
Opex-to-sale	22.0	21.0	19.5	(2.5)	(1.9)	22.0	21.5	19.3	(2.1)
Operating profit	461	495	525	14	(58)	461	956	731	(24)
OPM (%)	5.5	4.9	5.2	(0.3)	(2.9)	5.5	5.2	3.7	(1.5)
PBT	576	676	610	6	(68)	576	1,252	830	(34)
<b>Net profit</b>	<b>518</b>	<b>619</b>	<b>571</b>	<b>10</b>	<b>(70)</b>	<b>518</b>	<b>1,137</b>	<b>759</b>	<b>(33)</b>
NPM (%)	6.2	6.2	5.7	(0.5)	(4.3)	6.2	6.2	3.8	(2.4)

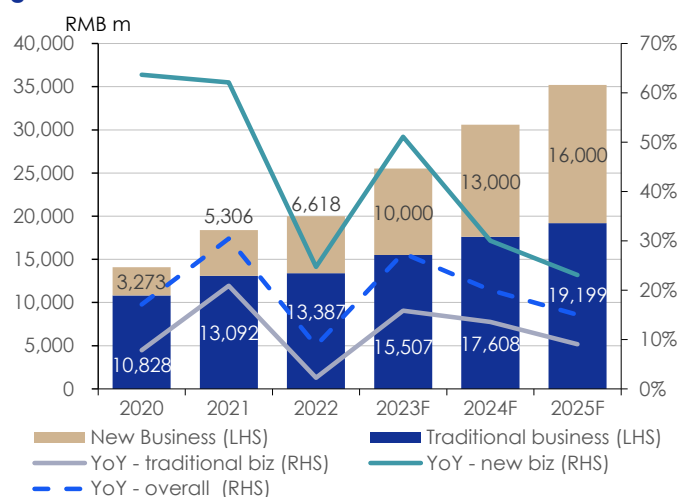
Source: Company, CCBIS

## Chinasoft – CCBIS earnings forecast revisions

P/L (RMB m)	New forecast			Previous forecast			Change (%)		
	2023F	2024F	2025F	2023F	2024F	2025F	2023F	2024F	2025F
Revenue	25,507	30,608	35,199	27,376	32,852	N/A	(6.8)	(6.8)	N/A
Gross profit	6,122	7,499	8,800	6,981	8,541	N/A	(12.3)	(12.2)	N/A
Opex	(4,974)	(5,969)	(6,864)	(5,544)	(6,652)	N/A	(10.3)	(10.3)	N/A
Operating profit	1,148	1,530	1,936	1,437	1,889	N/A	(20.1)	(19.0)	N/A
Net profit	1,317	1,666	2,035	1,564	1,948	N/A	(15.7)	(14.5)	N/A
<b>%</b>									
Gross margin	24.0	24.5	25.0	25.5	26.0	N/A	(1.5)	(1.5)	N/A
OPEX to sales	(19.5)	(19.5)	(19.5)	(20.3)	(20.3)	N/A	0.7	0.8	N/A
OPM	4.5	5.0	5.5	5.3	5.7	N/A	(0.8)	(0.7)	N/A
Net margin	5.2	5.4	5.8	5.7	5.9	N/A	(0.5)	(0.5)	N/A

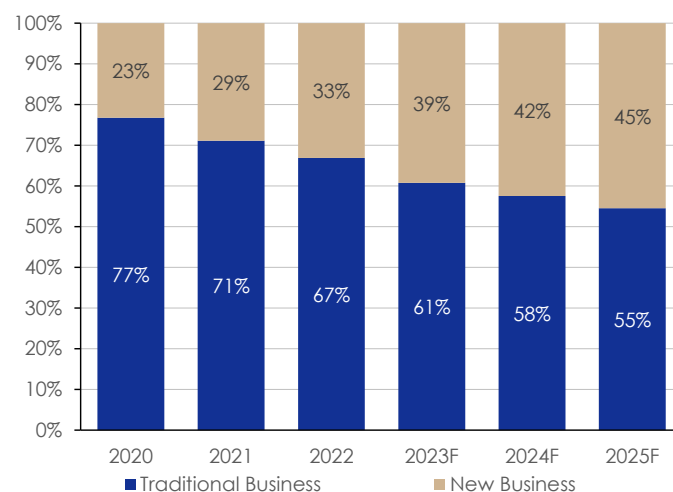
Source: CCBIS estimates

## Chinasoft – expect new businesses to deliver strong growth momentum



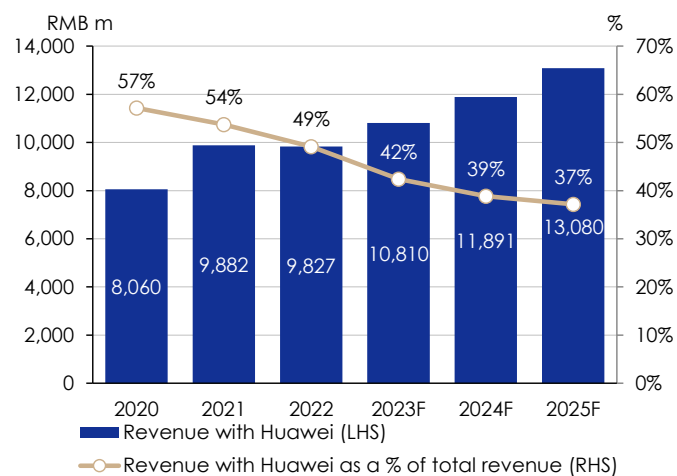
Source: Company, CCBIS estimates

## Chinasoft – increasing revenue contribution from new businesses



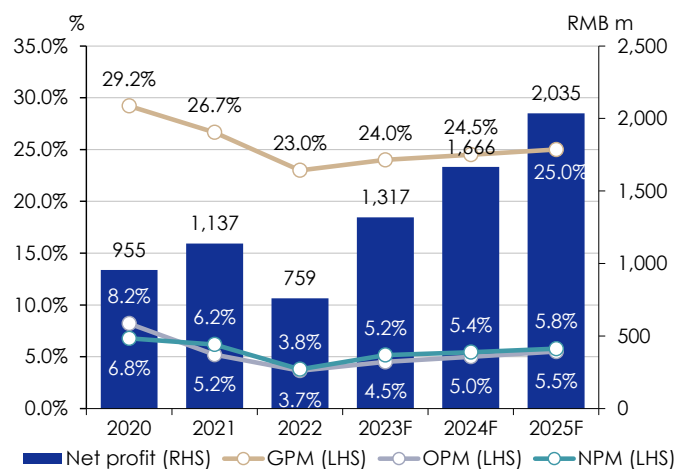
Source: Company, CCBIS estimates

### Chinasoft – revenue contribution from Huawei



Source: Company, CCBIS estimates

### Chinasoft – net income and margin ratios



Source: Company, CCBIS estimates

**Chinasoft Intl. – income statement forecast**

RMB m	FY21	FY22	FY23F	FY24F	FY25F	1H22	2H22	1H23F	2H23F
<b>Revenue breakdown</b>									
Traditional business	13,092	13,387	15,507	17,608	19,199	6,815	6,572	8,030	7,476
New business	5,306	6,618	10,000	13,000	16,000	3,210	3,408	4,000	6,000
<b>Total revenue</b>	<b>18,398</b>	<b>20,005</b>	<b>25,507</b>	<b>30,608</b>	<b>35,199</b>	<b>10,025</b>	<b>9,980</b>	<b>12,030</b>	<b>13,476</b>
YoY (%)	30	9	28	20	15	20	(1)	20	35
Cost of revenues	(13,494)	(15,405)	(19,385)	(23,109)	(26,399)	(7,544)	(7,861)	(9,203)	(10,182)
<b>Gross profit</b>	<b>4,904</b>	<b>4,600</b>	<b>6,122</b>	<b>7,499</b>	<b>8,800</b>	<b>2,482</b>	<b>2,118</b>	<b>2,827</b>	<b>3,294</b>
GPM (%)	26.7	23.0	24.0	24.5	25.0	24.8	21.2	23.5	24.4
S&M	(943)	(949)	(1,275)	(1,530)	(1,760)	(511)	(438)	(602)	(674)
G&A	(1,756)	(1,683)	(2,168)	(2,602)	(2,992)	(1,445)	(237)	(1,023)	(1,145)
R&D	(1,249)	(1,238)	(1,530)	(1,836)	(2,112)	0	(1,238)	(722)	(809)
Total operating expenses	(3,948)	(3,870)	(4,974)	(5,969)	(6,864)	(1,957)	(1,913)	(2,346)	(2,628)
<b>Operating profit</b>	<b>956</b>	<b>731</b>	<b>1,148</b>	<b>1,530</b>	<b>1,936</b>	<b>525</b>	<b>206</b>	<b>481</b>	<b>667</b>
OPM (%)	5.2	3.7	4.5	5.0	5.5	5.2	2.1	4.0	4.9
Other income, gains and losses	571	382	450	450	450	210	173	200	250
Allowance for doubtful debts	(112)	(89)	0	0	0	0	(89)	0	0
Other expenses	(48)	(55)	(50)	(50)	(50)	(27)	(28)	(25)	(25)
Finance costs	(100)	(113)	(100)	(100)	(100)	(52)	(61)	(50)	(50)
Share of results of associates	(10)	(23)	0	0	0	0	(23)	0	0
<b>Profit before tax</b>	<b>1,252</b>	<b>830</b>	<b>1,448</b>	<b>1,830</b>	<b>2,236</b>	<b>610</b>	<b>219</b>	<b>606</b>	<b>842</b>
Taxation	(115)	(71)	(130)	(165)	(201)	(40)	(31)	(55)	(76)
Effective tax rate (%)	(9.2)	(8.6)	(9.0)	(9.0)	(9.0)	(6.5)	(14.3)	(9.0)	(9.0)
Net income	1,137	759	1,317	1,666	2,035	571	188	552	766
- Minority interests	0	(1)	0	0	0	0	(1)	0	0
<b>Net income attributable to common shareholders</b>	<b>1,137</b>	<b>759</b>	<b>1,317</b>	<b>1,666</b>	<b>2,035</b>	<b>571</b>	<b>189</b>	<b>552</b>	<b>766</b>
YoY (%)	19	(33)	73	26	22	10	(70)	(3)	306
NPM (%)	6.2	3.8	5.2	5.4	5.8	5.7	1.9	4.6	5.7
Diluted EPS (RMB)	0.38	0.25	0.44	0.55	0.67	0.19	0.06	0.18	0.25
Diluted EPS (HK\$)	0.46	0.29	0.51	0.66	0.80	0.23	0.07	0.21	0.30
Diluted share volumes (m)	2,961	3,016	3,016	3,016	3,016	3,056	3,016	3,016	3,016
<b>Key ratios (%)</b>									
EPS growth	19	(37)	74	30	22	6	(72)	(7)	327
GPM	26.7	23.0	24.0	24.5	25.0	24.8	21.2	23.5	24.4
OPM	5.2	3.7	4.5	5.0	5.5	5.2	2.1	4.0	4.9
NPM	6.2	3.8	5.2	5.4	5.8	5.7	1.9	4.6	5.7
ROAE	11.2	6.4	10.4	11.8	12.8	N/A	N/A	N/A	N/A
Net debt/equity	Net cash	Net cash	Net cash	Net cash	Net cash	N/A	N/A	N/A	N/A

Source: Company, CCBIS estimates

## Chinasoft International | 354 HK – financial summary

### Profit and loss

FYE 31 Dec (RMB m)	2021	2022	2023F	2024F	2025F
TPG business	16,622	17,930	22,861	27,434	31,549
IIG business	1,776	2,075	2,645	3,174	3,651
<b>Revenue</b>	<b>18,398</b>	<b>20,005</b>	<b>25,507</b>	<b>30,608</b>	<b>35,199</b>
COGS	(13,494)	(15,405)	(19,385)	(23,109)	(26,399)
<b>Gross profit</b>	<b>4,904</b>	<b>4,600</b>	<b>6,122</b>	<b>7,499</b>	<b>8,800</b>
Operating expenses	(3,948)	(3,870)	(4,974)	(5,969)	(6,864)
<b>EBIT</b>	<b>956</b>	<b>731</b>	<b>1,148</b>	<b>1,530</b>	<b>1,936</b>
Net financial income (exp.)	(100)	(113)	(100)	(100)	(100)
Other	396	212	400	400	400
<b>Profit before tax</b>	<b>1,252</b>	<b>830</b>	<b>1,448</b>	<b>1,830</b>	<b>2,236</b>
Tax	(115)	(71)	(130)	(165)	(201)
<b>Total profit</b>	<b>1,137</b>	<b>759</b>	<b>1,317</b>	<b>1,666</b>	<b>2,035</b>
<b>Net profit attributable to shareholders</b>	<b>1,137</b>	<b>759</b>	<b>1,317</b>	<b>1,666</b>	<b>2,035</b>
Reported EPS (HK\$)	0.46	0.29	0.51	0.66	0.80
Diluted EPS (RMB)	0.38	0.25	0.44	0.55	0.67
Dividend (RMB)(m)	70	80	112	125	153
Dividend per share (RMB)	0.02	0.03	0.04	0.04	0.05

### Cash flow

FYE 31 Dec (RMB m)	2021	2022F	2023F	2024F	2025F
<b>Profit before tax</b>	<b>1,252</b>	<b>830</b>	<b>1,448</b>	<b>1,830</b>	<b>2,236</b>
Amortization & depreciation	221	237	253	268	284
Net financial charge adj.	100	113	100	100	100
Non-cash items adjusted	95	–	–	–	–
Change in working capital	(887)	(800)	(1,191)	(1,482)	(1,342)
Tax paid	(20)	(71)	(130)	(165)	(201)
Other	–	(467)	–	–	–
<b>Operating cash flow</b>	<b>761</b>	<b>(158)</b>	<b>479</b>	<b>552</b>	<b>1,076</b>
Capex	(438)	(160)	(160)	(160)	(160)
Investment	(160)	–	–	–	–
Interest received	40	–	–	–	–
Other	29	(50)	(50)	(50)	(50)
<b>Investment cash flow</b>	<b>(530)</b>	<b>(210)</b>	<b>(210)</b>	<b>(210)</b>	<b>(210)</b>
Change in borrowings	173	–	–	–	–
Equity issues	1,629	–	–	–	–
Interest paid	(70)	(113)	(100)	(100)	(100)
Dividend paid	(70)	(70)	(80)	(112)	(125)
Other	(226)	–	–	–	–
<b>Financing cash flow</b>	<b>1,435</b>	<b>(183)</b>	<b>(180)</b>	<b>(212)</b>	<b>(225)</b>
<b>Change in cash flow</b>	<b>1,666</b>	<b>(551)</b>	<b>90</b>	<b>130</b>	<b>641</b>
Cash & equivalents, begin	3,787	5,556	5,005	5,095	5,225
Forex	(40)	–	–	–	–
<b>Cash &amp; equivalents, end</b>	<b>5,413</b>	<b>5,005</b>	<b>5,095</b>	<b>5,225</b>	<b>5,867</b>
<b>Free cash flow</b>	<b>323</b>	<b>(318)</b>	<b>319</b>	<b>392</b>	<b>916</b>

Source: Company, CCBIS estimates

### Balance sheet

FYE 31 Dec (RMB m)	2021	2022	2023F	2024F	2025F
Cash & equivalents	5,556	5,005	5,095	5,225	5,867
Pledge dep., restricted cash	16	45	45	45	45
Receivables	7,784	8,313	10,870	13,013	14,941
Inventory	163	99	99	99	99
Other current assets	–	138	138	138	138
<b>Total current assets</b>	<b>13,520</b>	<b>13,601</b>	<b>16,248</b>	<b>18,521</b>	<b>21,090</b>
Property, plant & equipment	1,220	1,119	1,084	1,038	982
Intangible assets	193	281	273	261	243
Other non-current assets	1,970	1,964	1,964	1,964	1,964
<b>Total non-current assets</b>	<b>3,383</b>	<b>3,364</b>	<b>3,322</b>	<b>3,263</b>	<b>3,189</b>
<b>Total assets</b>	<b>16,903</b>	<b>16,965</b>	<b>19,570</b>	<b>21,784</b>	<b>24,279</b>
Short-term borrowings	917	766	766	766	766
Trade & bills payable	2,252	2,049	3,416	4,076	4,662
Other current liabilities	817	739	739	739	739
<b>Total current liabilities</b>	<b>3,986</b>	<b>3,553</b>	<b>4,920</b>	<b>5,581</b>	<b>6,167</b>
Long-term borrowings	1,021	1,162	1,162	1,162	1,162
Other non-current liabilities	269	114	114	114	114
<b>Total non-current liabilities</b>	<b>1,290</b>	<b>1,277</b>	<b>1,277</b>	<b>1,277</b>	<b>1,277</b>
<b>Total liabilities</b>	<b>5,276</b>	<b>4,830</b>	<b>6,197</b>	<b>6,858</b>	<b>7,444</b>
Share capital	6,432	6,151	6,151	6,151	6,151
Reserves and retained profits	5,172	5,959	7,197	8,751	10,660
<b>Shareholders' equity</b>	<b>11,604</b>	<b>12,110</b>	<b>13,348</b>	<b>14,901</b>	<b>16,811</b>
Minority interest	23	25	25	25	24
<b>Total equity</b>	<b>11,627</b>	<b>12,135</b>	<b>13,373</b>	<b>14,926</b>	<b>16,835</b>
<b>Total equity and liabilities</b>	<b>16,903</b>	<b>16,965</b>	<b>19,570</b>	<b>21,784</b>	<b>24,279</b>

### Ratios

FYE 31 Dec	2021	2022	2023F	2024F	2025F
<b>Growth (%)</b>					
Revenue	30.5	8.7	27.5	20.0	15.0
EBITDA	(11.3)	(17.8)	44.7	28.4	23.4
EBIT	(17.4)	(23.6)	57.1	33.3	26.5
Net profit	19.1	(33.2)	73.5	26.4	22.2
<b>Profitability (%)</b>					
Gross margin	26.7	23.0	24.0	24.5	25.0
EBITDA margin	6.4	4.8	5.5	5.9	6.3
EBIT margin	5.2	3.7	4.5	5.0	5.5
Net margin	6.2	3.8	5.2	5.4	5.8
Tax rate	9.2	8.6	9.0	9.0	9.0
<b>Efficiency (days)</b>					
Inventory turnover	3	3	2	2	1
Trade receivables	104	111	100	101	103
Trade payables	55	51	51	59	60
<b>Returns &amp; leverage (%)</b>					
ROAA	7.6	4.5	7.2	8.1	8.8
ROAE	11.2	6.4	10.4	11.8	12.8
Net debt (cash)/equity	(31.1)	(25.4)	(23.7)	(22.1)	(23.4)
<b>Liquidity (x)</b>					
Current ratio	3.4	3.8	3.3	3.3	3.4
Quick ratio	3.4	3.8	3.3	3.3	3.4

**Rating definitions:****Outperform (O) – expected return > 10% over the next twelve months****Neutral (N) – expected return between -10% and 10% over the next twelve months****Underperform (U) – expected return < -10% over the next twelve months****Analyst certification:**

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