

Xiaomi Corporation (1810 HK)

Headwind ahead; initiate with HOLD

- Xiaomi ("the Group" or "Xiaomi") showed a slower smartphone shipment growth in recent quarter.
- We forecast operating margin to be 5.7%/ 5.3%/ 5.2% in FY19E-21E, due to the rise in R&D expenses.
- We expect the Group's shareholders' profit to grow by -15.7%/17.4%/16.8% for FY19E-FY21E
- Initiate **HOLD** with TP of HK\$11.50, which implies 15.5x FY19E P/E ratio

We project the Group's overall revenue to grow by 30.3%/ 26.3%/ 20.2% in FY19E-FY21E based on our estimates of smartphones shipments, IoT & lifestyle products and internet services revenues. The proportion of smartphone revenue is expected to decrease with higher contributions from IoT & lifestyle products and internet services.

Gross profit margin is dragged down from weaker smartphone margin. We forecast gross profit margin to lower by 0.3ppt / 0.1ppt/ 0.1ppt to 12.4%/ 12.3%/ 12.2% in FY19E-FY21E. The lowering in smartphone gross margin will affect the overall gross margin.

Shifting to a more internet-oriented business. Xiaomi is shifting its business focus towards internet services due to the slowdown in smartphone shipments with market saturation and stiff competition. However, uncertainty regarding the Group's development in the internet business remains high given that the China's internet sector is fiercely competitive.

Recommend HOLD. Due to limited upside potential, we initiate **HOLD** on Xiaomi with the TP of HK\$11.50, implying 15.5x FY19E P/E ratio.

Results and Valuation

FY ended Dec 31	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue (RMB mn)	114,625	174,915	227,889	287,893	346,116
Chg (% YoY)	67.5	52.6	30.3	26.3	20.2
Shareholders' profit (RMB mn)	(43,826)	13,554	11,425	13,412	15,668
Chg (% YoY)	N/A	N/A	(15.7)	17.4	16.8
Non-IFRS adjusted					
Shareholders' profit (RMB mn)	5,362	8,555	9,966	10,694	11,207
Chg (% YoY)	182.9%	59.5%	16.5%	7.3%	4.8%
EPS (RMB)	(4.49)	0.84	0.66	0.78	0.91
Chg (% YoY)	N/A	N/A	(15.7)	17.4	16.8
BPS (RMB)	(13.04)	4.44	4.79	5.56	6.47
Chg (% YoY)	N/A	N/A	0.1	0.2	0.2
P/E (x)	N/A	11.5	14.8	12.6	10.8
P/B (x)	N/A	2.2	2.0	1.8	1.5
ROE (%)	34.4	19.0	13.8	13.9	14.0
ROA (%)	(48.8)	9.3	7.1	7.5	7.8

Source(s): Bloomberg, ABCI Securities estimates

*Exchange rate assumption for FY19E-21E: HKD 1 = RMB 0.890

Initiation Report

Initiation

May 7, 2019

Rating: Hold
TP: HK\$11.50

Analyst: Ricky Lai

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Share price (HK\$)	11.00
Est. share price return	4.5%
Est. dividend yield	0.0%
Est. total return	4.5%

Source(s): Bloomberg, ABCI Securities

Key Data

52Wk H/L(HK\$)	22.2/9.4
Issued shares (mn)	23,970.5
Class B (listed)	17,280.9
Class A (unlisted)	6,689.6
Class B Market cap (HK\$ mn)	190,089.9
Avg daily turnover (HK\$ mn)	1,192.5
Major shareholder(s) of class B shares:	
Lou Titing	16.8%
Shi Jianming	16.8%
Liu Qin	16.2%

Source(s): Company, ABCI Securities

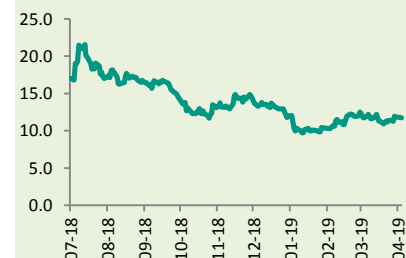
Share Performance (%)

	Absolute	Relative*
1-mth	(3.0)	(6.8)
3-mth	14.5	1.4
6-mth	(6.5)	(21.5)

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

Share performance (HK\$)



Source(s): Bloomberg, ABCI Securities



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Global Smartphone Industry Competitive Landscape

According to IDC, global smartphone shipments declined by 6.6% YoY to 310.8 mn in 1Q19. Smartphone shipments were affected by longer phone replacement cycle, limited innovative features from new phones, and increasing penetration rate. The top five smartphone shipments makers were Samsung, Apple, Huawei, Vivo, and Xiaomi. Chinese smartphone makers are accounting for a significant proportion of smartphone shipments in the market, showing that the Chinese brands are becoming important players in the field.

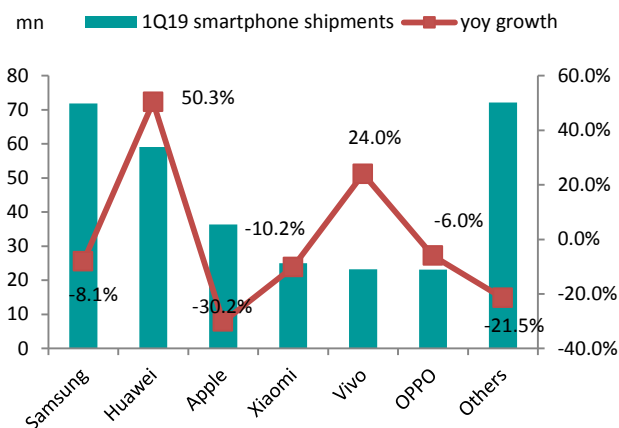
The smartphones shipments growth of Chinese brands (Huawei's +50.3%, Vivo's +24.0%) were above the market average of -6.6% in 1Q19.

Huawei's smartphone shipments surged 50.3% YoY to 59.1 mn in 1Q19 with a 19.0% market share, making it the second-largest smartphone producer in the world after Samsung. Huawei has improved its brand reputation with the alliance with large corporations and sponsored celebrities.

Samsung's shipments fell 8.1% YoY to 71.9 mn in 1Q19 and its market share dipped to 23.1% due to weaker product shipments to the China market. Apple's iPhone shipments slipped 30.2% YoY to 36.4mn in 1Q19 with a market share of 11.7%. The latest release of iPhone in 2018 disappointed the market with little innovation and high selling price. The global smartphone shipments were affected by the slowing demand from China. It is estimated smartphone shipments will further be lowered in 2019 with market saturation and longer replacement cycle.

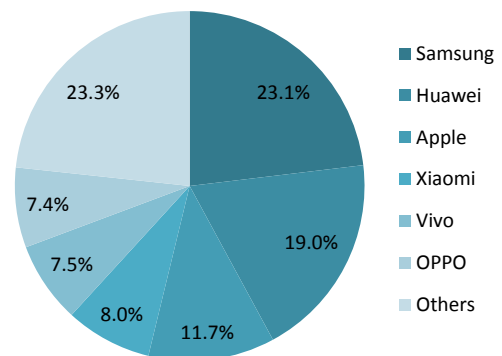
For the China market, Huawei shipped the most number of smartphones in 1Q19, driven by the launch of flagship models (P20) that introduced a number of new features including multi-camera, face recognition, AI technology, ultra-thin bezel, etc.

Exhibit 1: Global smartphone shipments in 1Q19



Source(s): IDC.

Exhibit 2: Global smartphone market share in 1Q19



Source(s): IDC.



Company Overview

Xiaomi Corporation (“the Group” or “Xiaomi”) offers a wide range of products and services including smartphones, internet services, electronic hardware devices, and home accessories. The Group was founded in 2010 and its Class B ordinary shares were listed on the HKEx main board in 2018.

The Group distributes its products and services through online stores and offline stores (Mi Homes) that allow consumers to acquire first-hand product experiences. The Group’s revenue was mainly generated from the China market (60.0%) in FY18, compared to 72.0% in FY17. The overseas market is becoming an increasingly important source of Xiaomi’s revenue thanks to its expansion strategy.

The Group generates its revenue from four segments: (1) smartphones; (2) IoT & lifestyle services; (3) internet services; & (4) others

Exhibit 3: The Group’s milestones

Date	Events
2010	Founded in China
2014	Reached number one smartphone market share in China
2015	MIUI MAU exceeded 100 mn
2017	The world’s largest consumer IOT platform in terms of connected devices (excluding smartphones and laptops)
2018	Partnered with CK Hutchison (1HK) for products distributions in retail stores
2018	Listed on the main board of HKEx
2018	Strategic partnership with Meitu (1357 HK) to launch smartphones
2018	Co-operated with TCL corporation (100 SZ) for R&D in smart hardware and core electronics components

Source(s): the Group, ABCI Securities

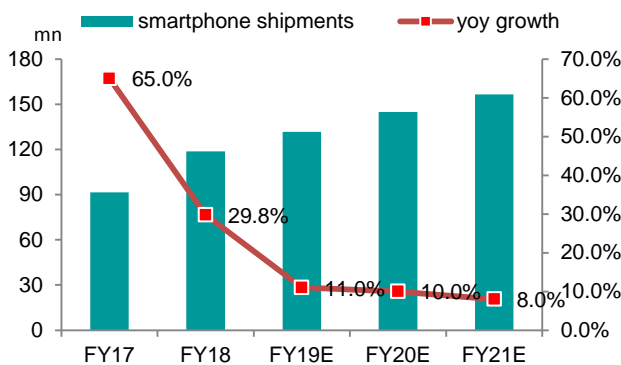
1. Smartphone business

The Group generated most of its revenue from smartphones (65%) in FY18. The Group has two smartphone brands, Mi and Redmi, targeting for different market segments. Xiaomi smartphones are famous for its low price and competitive quality. Recently, the Group has entered the high-end market with the launch of Mi9 with triple camera and under screen finger print sensor. The Group has won a number of recognition for its smartphones, including the “China Quality Technical Award”, the “2018 People’s Ingenuity Product Award”, and the “2018 China Quality Benchmark Prize”.

Revenue generated from products priced at RMB 2,000 or above accounted for 31.8% of total revenue in the smartphone segment in FY18. Xiaomi’s smartphone ASP grew 8.8% YoY to RMB 958.7 in FY18, driven by the launch of flagship smartphones, including Mi 8 and Mi MIX 3 in 2018, and better brand recognition.

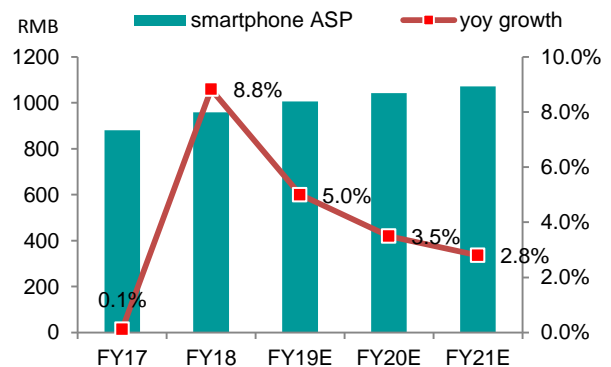
In 1Q19, the Group has launched a new flagship smartphone Mi 9 with good market response, which is set to further improve its smartphone ASP. Xiaomi’s 5G smartphone Mi MIX3 5G will be launched in FY19 to meet market demand. We expect Xiaomi’s smartphone revenue to grow 16.6%/13.9%/11.0% in FY19E-20E, based on our estimations of smartphone shipments and ASP.

Exhibit 4: The Group’s smartphone shipments and YoY growth



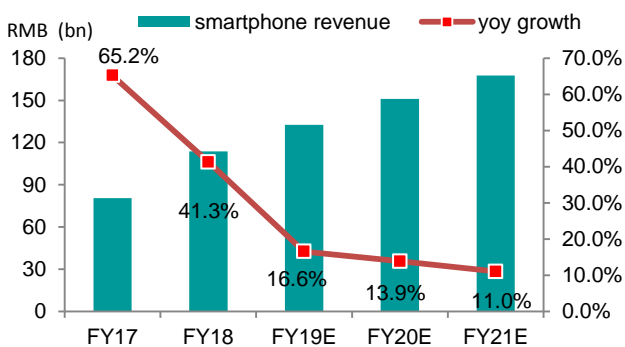
Source(s): the Group, ABCI Securities estimates

Exhibit 5: The Group’s smartphone ASP and YoY growth



Source(s): the Group, ABCI Securities estimates

Exhibit 6: The Group’s smartphone revenue and YoY growth



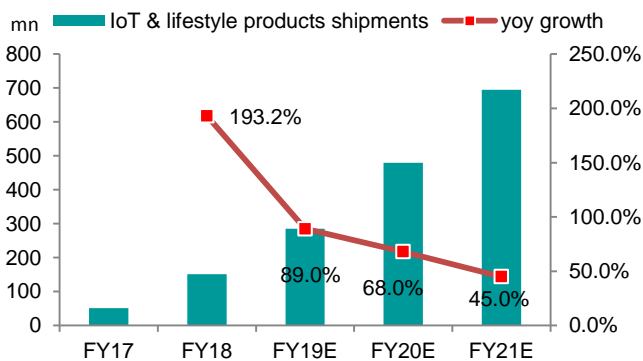
Source(s): the Group, ABCI Securities estimates

2. IoT & lifestyle products segment

The IoT & lifestyle products segment generated the second largest revenue for the Group (25.1% in FY18), with the distribution of smart devices and home appliances such as conditioner, washing machine, laptops, vacuum cleaner, etc. The Group offers a smart device ecosystem by connecting devices through its software platform Mi Home (20.3 mn MAU). By using the AI technology, Xiaomi can enhance devices efficiency and improve user experiences.

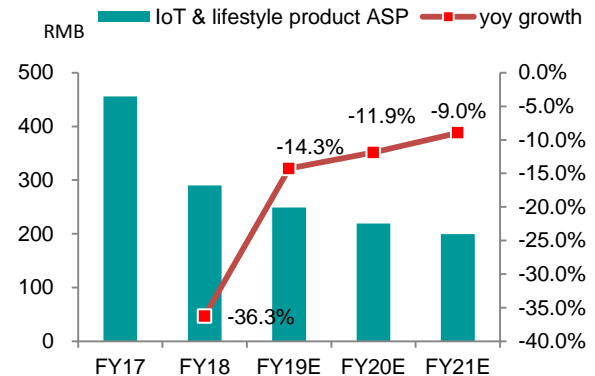
According to iResearch, the number of global IoT end points is expected to reach 15.3bn in 2020, representing a CAGR of 25.4% in 2017-20. The large user base of IoT devices would allow Xiaomi to improve product shipment and app user base for monetization. It will launch more varieties of lifestyle devices and smart products to meet consumers' preferences of better living standard with a competitive pricing strategy. There are a number of competitors in the sector including TCL electronics (1070 HK), Haier (1169 HK), Skyworth Digital (751 HK), Midea (333 CH), which have a much larger scale and cost advantage compared to Xiaomi. There were 285.2mn shipments for the Group's IoT & lifestyle products, up 89.0% YoY, but ASP decreased by 14.3% YoY to RMB 248.9 in FY18. We project IoT & lifestyle products revenue to grow by 62.0%/ 48.0%/ 32.0% in FY19E-21E.

Exhibit 7: The Group's IoT & lifestyle products shipments and YoY growth



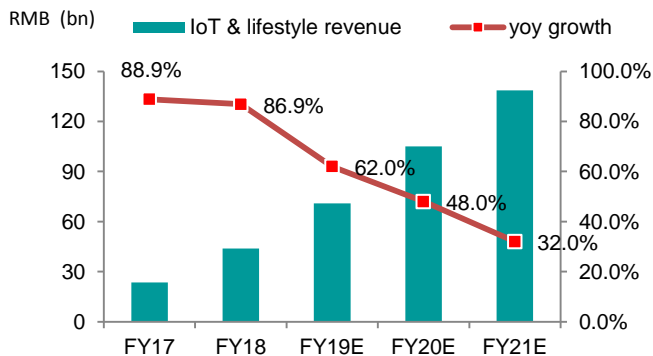
Source(s): the Group, ABCI Securities estimates

Exhibit 8: The Group's IoT & lifestyle products ASP and YoY growth



Source(s): the Group, ABCI Securities estimates

Exhibit 9: The Group's IoT & lifestyle products revenue and YoY growth



Source(s): the Group, ABCI Securities estimates

3. Internet services segment

The Group generates its internet services revenue by operating app stores, game center, contents, internet finance, and e-commerce services.

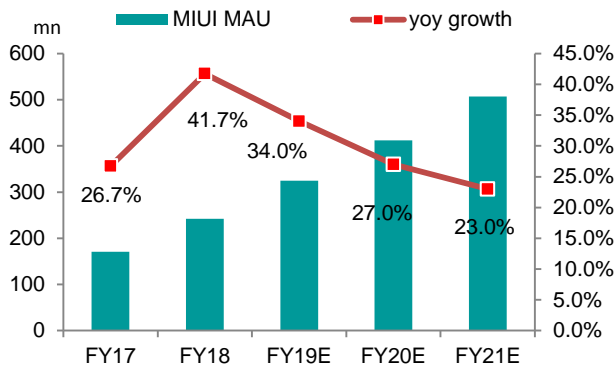
Internet services revenue grew 61.2% YoY, which accounted for 9.1% of total revenue in FY18 (+0.5ppt YoY). The Group has its smartphones pre-installed with self-developed apps which help raise user base and improve adoption at a relatively low user acquisition cost. The Group's smartphones can act as an effective gateway for allowing users to access its internet apps and boost internet services revenue growth. Internet services revenue is mainly composed of advertising services revenue and internet value-added services revenue. The advertising services revenue contributed to 63.0% of total internet services revenue in FY18, up 6.3ppt YoY, thanks to the growing mobile app user base; the value-added services revenue contributed to 37.0% of total internet services revenue in FY18.

The Group generated its advertising service revenue from its app store, advertisement inside app, and content apps. For the value-added services, it offers the internet finance services through Xiaomi wallet, Xiaomi finance and Xiaomi Loan apps, which allow users to apply for personal loan and Xiaomi hardware installment loan services. The user growth of MIUI, Xiaomi's mobile operating system built on the Android kernel platform, is closely related to Xiaomi's smartphone shipments because smartphones provide an effective entrance and platform for growing MIUI users.

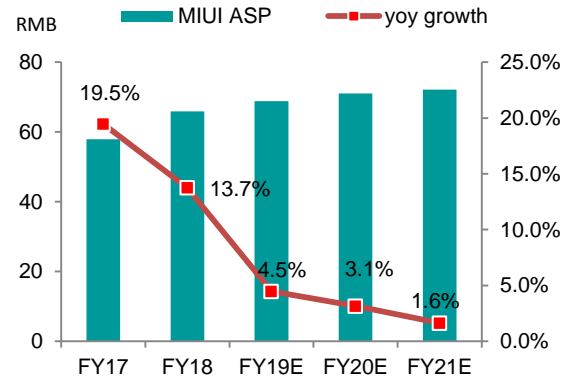
According to iResearch, global internet services revenue is estimated to reach US\$ 2,600.9 bn by 2022, representing a CAGR of 11.0% in 2017-20, driven by increasing mobile internet penetration. Internet services revenue surged 61.2% in FY18, compared to 51.4% in FY17, driven by robust user growth and ASP improvement. The MAU of MIUI increased 41.7% YoY to 242.1mn in FY18. Internet services ASP improved by 13.7% YoY to RMB 65.9.

The internet sector in China is highly competitive - the three largest internet companies (Tencent, Alibaba, and Baidu) have huge user bases and resources allocations. Xiaomi's smartphone users can choose to use apps by other internet companies instead of Xiaomi's. We forecast internet services revenue to grow by 40.0%/ 31.0%/ 25.0% in FY19E-FY21E.

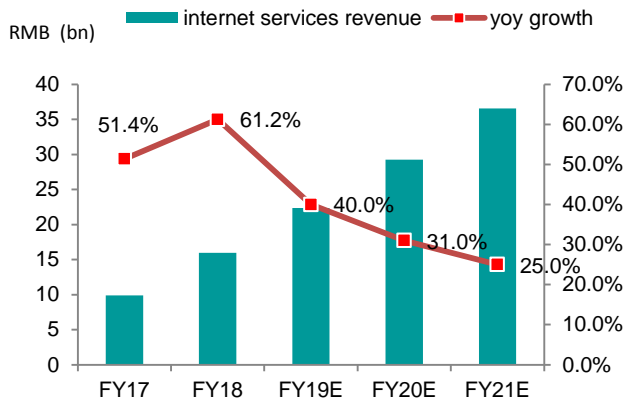
We project the Group's overall revenue to grow by 30.3%/ 26.3%/ 20.2% in FY19E-FY21E based on our estimates of smartphones shipments, IoT & lifestyle products and internet services revenues. The proportion of smartphone revenue is expected to decrease with higher contributions from IoT & lifestyle products and internet services.

Exhibit 10: The Group's MIUI MAU and YoY growth


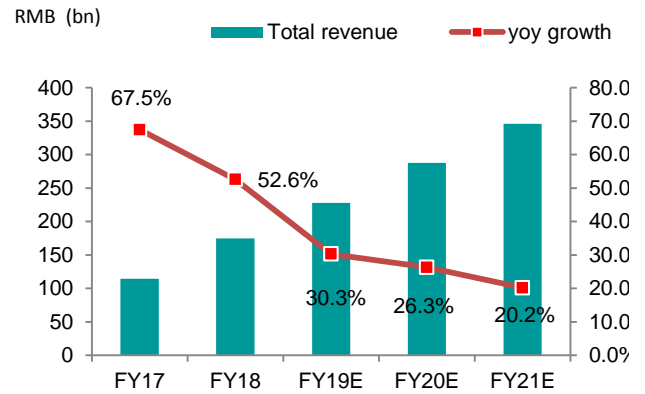
Source(s): the Group, ABCI Securities estimates

Exhibit 11: The Group's MIUI ASP and YoY growth


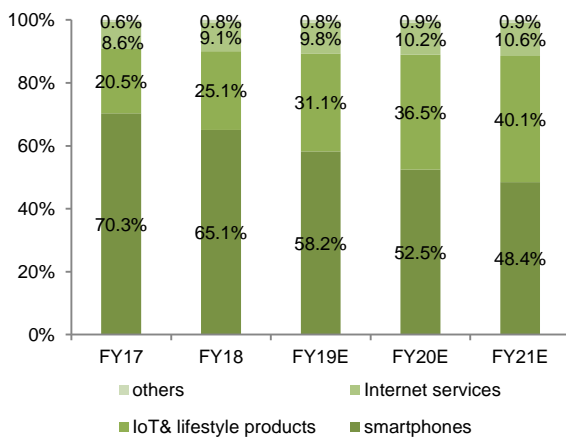
Source(s): the Group, ABCI Securities estimates

Exhibit 12: The Group's internet services revenue and YoY growth


Source(s): the Group, ABCI Securities estimates

Exhibit 13: The Group's total revenue and YoY growth


Source(s): the Group, ABCI Securities estimates

Exhibit 14: The Group's revenue breakdown


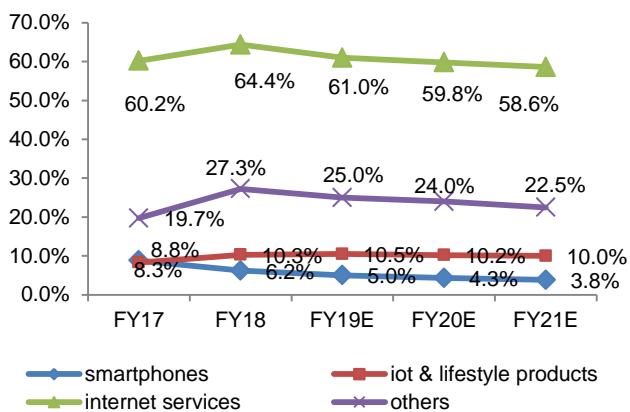
Source(s): the Group, ABCI Securities estimates

Profit margin analysis

The Group's overall gross profit margin declined by 0.5ppt YoY to 12.7% in FY18 mainly due to the decrease in smartphone gross profit. FY18 smartphone gross margin decreased because of increased costs associated with the sales of smartphones.

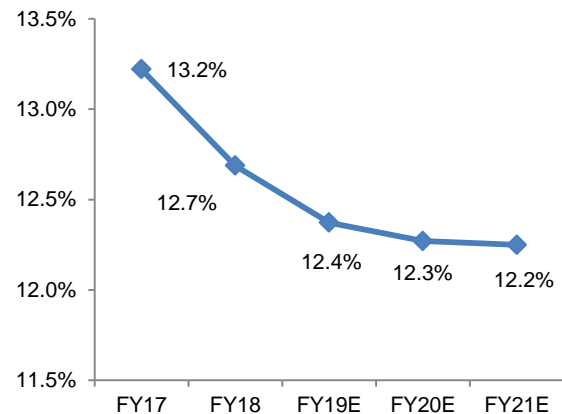
The internet services had the highest gross margin in FY18 with 64.4%, compared to smartphones' 6.2%, IoT & lifestyle products' 10.3% and others' 27.3%. However, the internet services just accounted for 9.1% of total revenue in FY18 for the Group. We expect smartphones gross margin to further weaken in FY19E with higher inventory costs, third-party intellectual property costs, and warranty expenses. As smartphone still contributes to a significant proportion of overall revenue, we project overall gross margin to lower by 0.3ppt/ 0.1ppt/ 0.1ppt to 12.4%/ 12.3%/ 12.2% in FY19E-21E.

Exhibit 15: The Group's gross profit margin breakdown



Source(s): the Group, ABCI Securities estimates

Exhibit 16: The Group's overall gross profit margin

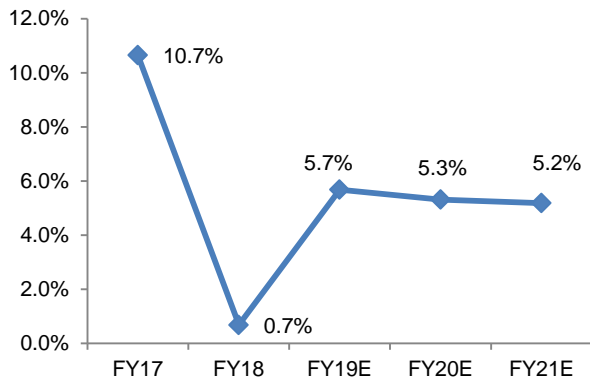


Source(s): the Group, ABCI Securities estimates

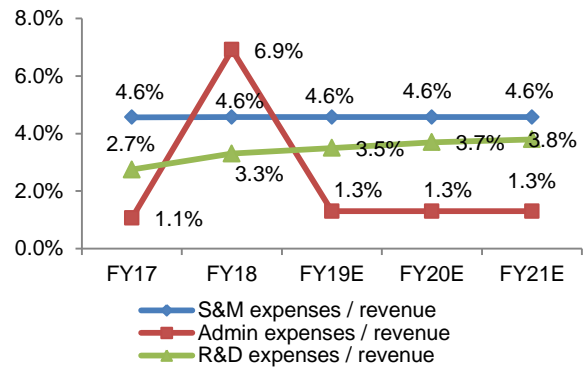
Operating profit margin lowered from 10.7% in FY17 to 0.7% in FY18, mainly due to the drag from higher admin expenses with one-off share-based compensation expenses. Admin expenses increased 894.9% YoY to RMB 12.1bn in FY18 due to the one-off share based compensation expenses. Excluding the compensation expense in FY18, Xiaomi's admin expenses grew 4.8% YoY instead. S&M expenses, as a percentage of revenue, was 4.6%, flat YoY. Xiaomi uses O2O distribution and channel marketing for sales and marketing. It distributes products through online store and retails, which helped to stabilize S&M expenses. We estimate such expenses, as a percentage of revenue, to remain stable at 4.6% in FY19E-21E.

R&D expenses, as a percentage of revenue, was 3.3% in FY18, up 0.6ppt YoY, due to higher spending for technology innovation and new feature introduction with the launch of new smartphone models. We expected the Group to raise its R&D expenses for 5G smartphones in FY19E with advanced features for smartphones. We expect R&D expenses, as a percentage of revenue, to increase 0.2ppt/ 0.2ppt/ 0.1ppt to 3.5%/ 3.7%/ 3.8% in FY19E-21E. We forecast operating margin to be 5.7%/ 5.3%/ 5.2% in FY19E-21E.

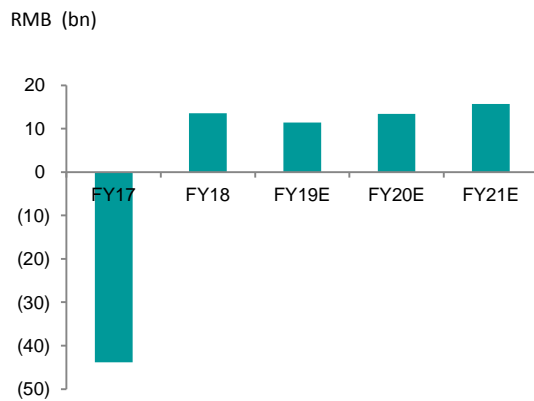
Based on our estimation of revenue and expenses forecasts, we expect the Group's shareholders' profit to grow by -15.7%/17.4%/16.8% for FY19E-FY21E.

Exhibit 17: The Group's operating profit margin


Source(s): the Group, ABCI Securities estimates

Exhibit 18: The Group's operating costs as a percentage of revenue


Source(s): the Group, ABCI Securities estimates

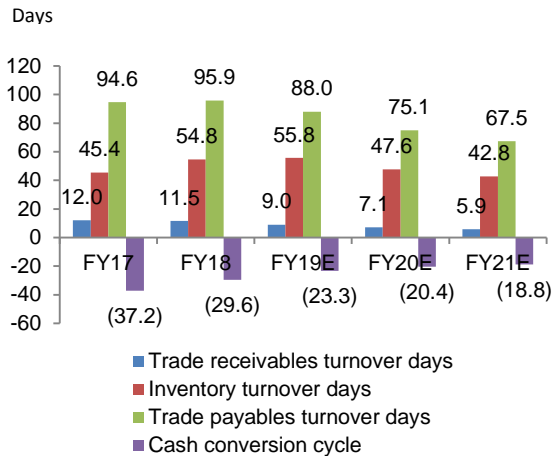
Exhibit 19: The Group's shareholders' profit


Source(s): the Group, ABCI Securities estimates

The Group's inventory turnover days increased from 45.4 in FY17 to 54.8 in FY18, which signaled that smartphone shipment has been slowing with inventories piling up. We forecast inventory turnover days to further increase to 55.8 in FY19E due to weaker smartphone demand with market saturation and fierce competition, but start to decrease in FY20E due to the launch of 5G telecom network with better replacement needs. Trade receivable days in FY18 was 11.5, compared to 12.0 in FY17. There was an improvement in trade receivable days. The slight improvement in trade receivable days can be attributed to scale effect and better credit terms with customers days due to scale effect and the Group is more able to have a better credit terms with customers.



Exhibit 20: The Group's turnover days



Source(s): the Group, ABCI Securities estimates

Recommend HOLD with TP at HK\$11.50

We apply SOTP (Sum of the total parts) method for the valuation of the Group because the Group has both hardware and internet segments. The SOTP method derives an EV of RMB222 bn to RMB275 bn with a fair equity value per share of HK\$12.9 to HK\$15.9. We apply a 10.9% discount to the lower end to obtain our TP of HK\$11.50 (implying 15.5x FY19E).

Xiaomi's smartphone market share and profit margin were much lower than Apple's and Samsung's. We value the Group's smartphone business at 8x to 12x FY19E P/E, lower than Apple's (17.4x FY19 P/E) and Samsung's (12.8x FY19 P/E).

The valuation of IoT & lifestyle product business stands at 7x to 9x FY19E P/E due to the Group's late entry to this segment and there are a number of well-established corporations (such as Skyworth Digital (751 HK), TCL (1070 HK), Midea (333 CH)) with better brands and cost advantage.

We estimate the value of internet service business to be 20x to 25x FY19E P/E, which is lower than the market average of 33.8%. Although Xiaomi has a solid smartphone user base, we believe it is difficult for it to compete with other Chinese internet corporations for monetization due to latter's domination in the field.



Exhibit 21: Xiaomi's SOTP valuation:

	FY19E core profit (RMB bn)	FY19E P/E multiple	EV (RMB bn)
Smartphone business	1,326	8x to 12x	10.6 to 15.9
IoT & lifestyle products business	710	7x to 9x	5.0 to 6.4
Internet services business	9,325	20x to 25x	186.5 to 233.1
Investments			20.0
Total			222.1 to 275.4

Source(s): the Group, ABCI Securities estimates

Exhibit 22: Peer Comparison Table

Ticker	Price*	Currency	P/E				P/B				ROE	ROA	EV/EBITDA	
			18A	19E	20E	21E	18A	19E	20E	21E	19E	19E	19E	
Handset companies														
Apple	AAPL US	208.48	USD	16.6	18.4	16.4	14.4	8.8	9.2	10.0	9.8	55.5	15.3	11.1
Samsung	5930 KS	45,300.00	WON	7.2	13.0	10.0	8.2	1.2	1.2	1.1	1.0	9.6	7.3	3.3
LG	3550 KS	74,100.00	WON	7.2	7.3	6.4	5.8	0.7	0.7	0.7	0.6	9.7	7.8	5.4
Lenovo	992 HK	6.82	HKD	n.a.	16.8	13.4	11.2	3.1	2.6	2.3	2.0	15.2	2.2	7.2
Xiaomi	1810 HK	11.00	HKD	11.6	19.9	14.9	10.9	3.4	2.7	2.3	1.9	13.9	6.8	16.8
Simple Average				10.6	15.1	12.2	10.1	3.4	3.3	3.3	3.1	20.8	7.9	8.8
Weighted Average				14.5	17.4	15.1	13.1	7.0	7.3	7.9	7.7	44.5	13.3	9.7
Internet companies														
Tencent	700 HK	375.60	HKD	39.6	33.3	26.3	21.6	10.1	7.4	5.9	4.8	23.2	11.6	24.8
Alibaba	BABA US	188.24	USD	48.8	36.3	29.4	22.5	8.2	6.6	5.7	4.6	17.4	8.0	26.3
Baidu	BIDU US	164.50	USD	14.3	20.6	15.1	12.0	2.5	2.2	1.9	1.7	10.6	5.3	15.3
Netease	NTES US	281.42	USD	38.0	27.2	22.6	20.5	5.5	4.3	3.7	3.3	14.6	8.5	18.2
Simple Average				35.2	29.3	23.4	19.2	6.6	5.1	4.3	3.6	16.5	8.3	21.1
Weighted Average				42.3	33.8	27.0	21.5	8.6	6.6	5.5	4.5	19.5	9.5	24.7
IoT & lifestyle														
Skyworth Digital	751 HK	2.12	HKD	14.6	7.4	6.2	4.5	0.4	0.5	0.4	0.3	5.2	2.0	n.a.
Tcl Electronics	1070 HK	3.93	HKD	10.4	9.7	8.5	8.2	1.1	1.1	1.0	0.9	10.9	3.4	2.8
Haier Electronics	1169 HK	21.65	HKD	14.1	12.8	11.4	10.2	2.4	1.9	1.7	1.5	17.8	9.2	7.2
Hisense Home	921 HK	10.34	HKD	9.6	8.2	7.3	6.6	1.9	1.6	1.3	1.1	18.1	6.6	n.a.
Midea Group	333 CH	49.07	CNY	16.9	15.2	13.4	12.2	4.1	3.5	3.1	2.7	24.1	8.9	11.1
Simple Average				12.7	11.5	10.2	9.3	2.3	2.0	1.8	1.6	17.7	7.0	7.0
Weighted Average				16.1	14.5	12.8	11.6	3.7	3.2	2.8	2.5	22.7	8.7	10.4

*Based on closing price on May 6, 2019

Source(s): Bloomberg



Risk factors

Fierce competition in internet services

The internet services sector in China is highly competitive with several giants dominating the market (including Alibaba (BABA US), Tencent (700 HK), and Baidu (BIDU US)). Xiaomi may have difficulties to monetize its platforms and apps as users can choose from many software developers.

Smartphone revenue growth is slowing down

Xiaomi's smartphone revenue growth was 41.3% in FY18, compared to 65.2% in FY17. The slowdown in smartphone revenue growth was due to weaker growth in smartphone shipment. Overall revenue growth is affected by the drag in weaker smartphone revenue growth due to its heavyweight contribution.

Subject to legal and administrative proceedings

Xiaomi is subjected to various legal, administrative proceedings and claims (such as being found to have infringed on intellectual property rights) that have arisen in the ordinary course of business and have not yet been fully resolved.

Internet services business may be affected by sector regulations

The internet sector in China is closely regulated and monitored by authorities. Xiaomi's gaming, video contents, e-commerce and advertising businesses may adversely affected by new and established rules and restrictions.

The use of non-IFRS item may have limitations

The use of non-IFRS adjusted net profit in our report may have limitations as an analytical tool, and should not consider them in isolation from, or as a substitute for analysis of, our results of operations or financial conditions as reported under IFRS.

The Group may record negative net operating cash flows in FY19 and FY20

Negative net operating cash flows were recorded in FY17 and FY18. In our projections, we expect the Group to record negative net operating cash flows in FY19 and FY20.



Financial Statements

Consolidated income statement (2017A-2021E)

FY Ended Dec 31 (RMB mn)	2017A	2018A	2019E	2020E	2021E
Smartphone revenue	80,564	113,800	132,634	151,004	167,651
IoT & lifestyle products revenue	23,448	43,817	70,983	105,055	138,673
Internet services revenue	9,896	15,956	22,338	29,262	36,578
Others	717	1,343	1,933	2,571	3,214
Total revenue	114,625	174,915	227,889	287,893	346,116
Gross profit	15,154	22,192	28,194	35,325	42,396
S&M expenses	(5,232)	(7,993)	(10,414)	(13,156)	(15,816)
Admin expenses	(1,216)	(12,099)	(2,963)	(3,743)	(4,500)
R&D expenses	(3,151)	(5,777)	(7,976)	(10,652)	(13,152)
Fair value changes on investments measured at fair value through profit or loss	6,371	4,430	5,772	7,292	8,767
Share of losses of investments accounted for using the equity method	(231)	(615)	(801)	(1,152)	(1,384)
Others	521	1,058	1,136	1,387	1,631
Operating Profits	12,215	1,196	12,948	15,302	17,941
Net finance costs	27	216	418	389	388
Fair value changes of convertible redeemable preferred shares	(54,072)	12,514	0	0	0
Profit before tax	(41,829)	13,927	13,366	15,690	18,329
Tax	(2,060)	(449)	(2,005)	(2,354)	(2,749)
Profit after tax	(43,889)	13,478	11,361	13,337	15,580
Minority interests	(63)	(76)	(64)	(75)	(88)
Shareholders' net profit	(43,826)	13,554	11,425	13,412	15,668
EPS (RMB)	(4.491)	0.843	0.661	0.776	0.907
non-IFRS adjusted net profit*	5,362	8,555	9,966	10,694	11,207

Source(s): the Group, ABCI Securities estimates

*The non-IFRS adjusted net profit exclude items of fair value changes of convertible redeemable preferred shares, share-based compensation, net fair value gains on investments, amortization of intangible assets resulting from acquisitions, changes of value of financial liabilities to fund investors



Consolidated balance sheet (2017A-2021E)

As of Dec 31 (RMB mn)	2017A	2018A	2019E	2020E	2021E
PPE	1,731	5,068	6,164	7,151	8,038
Long-term investments measured at fair value through profit or loss	18,857	18,636	30,054	41,601	53,259
Other non-current assets	8,143	15,511	16,349	17,261	18,253
Total non-current assets	28,731	39,215	52,568	66,013	79,550
Cash & cash equivalents	11,563	30,230	29,182	29,533	32,785
Inventories	16,343	29,481	31,544	34,383	36,790
Trade & loan receivables	13,614	15,892	16,304	16,732	17,177
Restricted cash	2,711	1,480	1,436	1,393	1,351
Others	16,907	28,929	30,247	31,660	33,171
Total current assets	61,138	106,013	108,713	113,701	121,274
Total assets	89,870	145,228	161,281	179,714	200,825
Trade payables	34,003	46,287	49,990	53,989	58,309
Borrowings	3,551	3,075	2,921	2,775	2,637
Others	9,579	12,578	13,415	14,322	15,306
Total current liabilities	47,133	61,940	66,326	71,087	76,251
Borrowings	7,251	7,856	8,170	8,497	8,837
Others	162,696	4,182	4,121	4,068	4,023
Total non-current liabilities	169,948	12,038	12,291	12,565	12,860
Total liabilities	217,080	73,978	78,617	83,652	89,110
Equity attributable to shareholders	(127,272)	71,323	82,748	96,160	111,828
Non-controlling interests	62	(73)	(85)	(98)	(114)
Total equity	(127,211)	71,250	82,664	96,062	111,714

Source(s): the Group, ABCI Securities estimates



Consolidated Cash Flow Statement (2017A-2021E)

As of Dec 31 (RMB mn)	2017A	2018A	2019E	2020E	2021E
Operating profit before change in working capital	7,811	23,842	8,589	10,664	13,041
Change in working capital	(7,283)	(23,699)	(8,565)	(9,364)	(8,955)
Tax	(1,523)	(1,558)	(1,594)	(1,631)	(1,668)
Operating cash flow	(996)	(1,415)	(1,570)	(331)	2,417
CAPEX	(1,218)	(1,096)	(986)	(888)	(799)
Others	(1,460)	(6,412)	532	578	628
Investing cash flow	(2,678)	(7,508)	(454)	(310)	(171)
Change in borrowings	6,644	129	160	181	201
Change in restricted cash	(289)	1,231	44	43	42
Others	(140)	25,214	(244)	(248)	(252)
Financing cash flow	6,215	26,574	(39)	(24)	(10)
Net increase in cash & cash equivalents	2,542	17,652	(2,063)	(665)	2,237
Cash & cash equivalents at beginning of year	9,230	11,563	30,230	29,182	29,533
Effect of changes in foreign exchange rate	(209)	1,015	1,015	1,015	1,015
Cash & cash equivalents at end of year	11,563	30,230	29,182	29,533	32,785
Financial Ratios:					
Gross margin (%)	13.2%	12.7%	12.4%	12.3%	12.2%
Operating margin (%)	10.7%	0.7%	5.7%	5.3%	5.2%
Net profit margin (%)	(38.2%)	7.7%	5.0%	4.7%	4.5%
ROA (%)	(48.8)	9.3	7.1	7.5	7.8
ROE (%)	34.4	19.0	13.8	13.9	14.0
YoY Growth:					
Revenue (%)	67.5%	52.6%	30.3%	26.3%	20.2%
Operating profit (%)	222.7%	(90.2%)	982.2%	18.2%	17.3%
Net profit (%)	(8021.6%)	(130.9%)	(15.7%)	17.4%	16.8%
Trade receivables turnover days	12.0	11.5	9.0	7.1	5.9
Inventory turnover days	45.4	54.8	55.8	47.6	42.8
Trade payable turnover days	94.6	95.9	88.0	75.1	67.5
Cash conversion cycle	(37.2)	(29.6)	(23.3)	(20.4)	(18.8)

Source(s): the Group, ABCI Securities estimates

Disclosures

Analyst Certification

I, Lai Pak Kin, Ricky, being the person primarily responsible for the content of this research report, in whole or in part, hereby certify that all of the views expressed in this report accurately reflect my personal view about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report. I and/or my associates do not serve as officer(s) of the listed company (ies) covered in this report.

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Definition of equity rating

Rating	Definition
Buy	Stock return rate \geq Market return rate (10%)
Hold	- Market return rate (-10%) \leq Stock return rate $<$ Market return rate (+10%)
Sell	Stock return $<$ - Market return (-10%)

Notes: Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months

Market return rate: average market return rate since 2005 (HSI total return index 2005-17 CAGR at 10%)

Time horizon of share price target: 12-month

Stock rating, however, may vary from the stated framework due to factors including but not limited to: corporate governance, market capitalization, historical price volatility relative to corresponding benchmark index, average daily turnover of the stock relative to market capitalization of the stock, competitive advantages in corresponding industry, etc.

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