CMB International Securities | Equity Research | Company Update

SANY Heavy Industry – A (600031 CH)

2Q20 net profit +78% in line; Strong rebound in cash flow

BUY (Maintain)

Target Price	**RMB26.40**
(previous TP	RMB24.70)
Up/Downside	**+16%**
Current Price	**RMB22.68**

SANY's net profit in 1H20 came in at RMB8.5bn, up 25.5% YoY. Net profit in 2Q20 surged 78% YoY to RMB6.3bn. In particular, operating cash inflow significantly rebounded to RMB9.4bn in 2Q, versus an outflow of RMB895mn in 1Q. While we fine-tuned our 2020E earnings forecast by -5% due mainly to lower assumption on the concrete machinery sales and the blended gross margin, we slightly raised our 2021E-22E earnings forecast by 1%, as we expect further operating cost reduction. We raised our TP from RMB24.7 to RMB26.4, based on 16x 2020E P/E (up from 14.3x), on the back of 16% estimated earnings growth in 2021E. SANY remains the key beneficiary of strong infrastructure spending growth and strict emission control policies. Reiterate **BUY.**

- **Key highlights on 1H20 results.** Revenue grew 13% YoY to RMB49bn, driven mainly by a 17% YoY increase in excavator revenue. Revenue from concrete machinery sales only increased by 5% YoY, slightly below our expectation. Gross margin narrowed by 2ppt YoY to 30.3%, which was largely due to the impact of COVID-19 in 1Q. SANY maintained a stringent expense control in 1H20, with S&D expense ratio reduced by 1.8ppt YoY. SANY maintained its R&D spending growth which we believe is essential for enhancing its long-term competitiveness. Net profit grew 25.5% YoY to RMB8.5bn.
- **Sharp recovery in 2Q20.** Revenue grew 45% YoY to RMB32bn in 2Q, a significant improvement from a decline of 19% in 1Q. While the gross margin was down 2.4ppt YoY to 31.5%, it improved 3.3ppt QoQ. All these, together with the increase in other gains and finance income, boosted net profit growth of 78% YoY (to RMB6.3bn) in 2Q compared with a decline of 32% YoY in 1Q. In particular, the operating cash inflow reached RMB9.4bn, suggesting excellent cash flow management.
- **High visibility on the 2H20E outlook**. According to CCMA, excavator sales volume (for the industry as a whole) grew 55% YoY in Jul. In addition, based on **Jiangsu Hengli's (601100 CH, BUY)** latest order intakes of hydraulic cylinders, we expect the momentum of excavator demand to continue over the coming months. Besides, we expect the concrete machinery sales growth to accelerate in 2H20E on the back of the recovery of property construction.
- **Key risks:** (1) Risk of overseas business due to pandemic; (2) Slowdown of construction activities; (3) Risk of expanding to financing business.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	55,822	75,666	90,868	99,635	105,517
YoY growth (%)	46	36	20	10	6
Net income (RMB mn)	6,116	11,207	13,962	16,288	17,589
EPS (RMB)	0.79	1.36	1.65	1.92	2.08
YoY growth (%)	189.6	71.4	21.8	16.7	8.0
Consensus EPS (RMB)	N/A	N/A	1.62	1.82	2.04
EV / EBITDA (x)	21.3	13.5	11.1	9.6	9.1
P/E (x)	28.7	16.7	13.7	11.8	10.9
P/B (x)	5.6	4.3	3.5	2.9	2.4
Yield (%)	1.2	1.9	2.3	2.7	2.9
ROE (%)	21.5	29.5	28.1	26.8	24.1
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIS estimates

China Capital Goods

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Stock Data

Mkt Cap (RMB mn)	192,163
Avg 3 mths t/o (RMB mn)	1,783
52w High/Low (RMB)	22.99/13.21
Total Issued Shares (mn)	8,435

Source: Bloomberg

Shareholding Structure

SANY Group	29.9%
Hong Kong CCASS	9.6%
Liang Wengen	3.4%
Others	57.1%

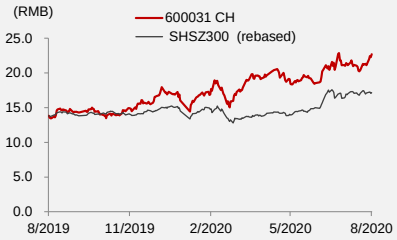
Source: Shanghai Stock Exchange

Share Performance

	Absolute	Relative
1-mth	5.5%	1.0%
3-mth	16.5%	-4.1%
6-mth	31.7%	13.9%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Ruihua CPA

Related Reports

1. China Construction Machinery & HDT Sector – Raise industry sales forecast in 2020E-21E; Solid upcycle – 30 Jun 2020
2. China Construction Machinery Sector – Four structural drivers to extend the upcycle to 2020-21E – 27 Nov 2019

Figure 1: Key highlights on 1H20 results

YE Dec 31(RMB mn)	1H19	1H20	Change (YoY)
Total revenue	**43,386**	**49,188**	*13.4%*
Cost of sales	(29,348)	(34,262)	*16.7%*
Gross profit	**14,039**	**14,925**	***6.3%***
Surcharge	(216)	(196)	*-9.5%*
S&D expenses	(3,011)	(2,546)	*-15.4%*
Administrative expenses	(2,097)	(2,582)	*23.1%*
Fair value change	255	282	*10.2%*
Asset impairment	(475)	(328)	*-30.9%*
EBIT	**8,495**	**9,555**	***12.5%***
Net finance income/(cost)	(11)	(7)	*-36.0%*
Finance income	261	280	*7.2%*
Finance expenses	(272)	(287)	*5.4%*
Other gains/(losses)	(250)	598	*-339.6%*
Share of profit of JV and associates	57	(22)	*-137.5%*
Pretax profit	**8,291**	**10,124**	***22.1%***
Income tax	(1,355)	(1,486)	*9.6%*
After tax profit	**6,936**	**8,638**	***24.5%***
MI	(188)	(171)	*-9.1%*
Net profit	**6,748**	**8,468**	***25.5%***
D&A	960	948	*-1.3%*
EBITDA	**9,455**	**10,503**	***11.1%***
Key ratios			*Change (ppt)*
Gross margin	*32.4%*	*30.3%*	*-2.0*
S&D expense ratio	*6.9%*	*5.2%*	*-1.8*
Administrative and R&D expense ratio	*4.8%*	*5.2%*	*0.4*
Net profit margin	*16.0%*	*17.6%*	*1.6*
Effective tax rate	*16.3%*	*14.7%*	*-1.7*

Source: Company data, CMBIS

Figure 2: Revenue and gross margin breakdown in 1H20 results

(RMB mn)	1H19	1H20	Change (YoY)
Revenue			
Concrete machinery	12,923	13,506	*4.5%*
Excavator	15,910	18,649	*17.2%*
Crane machinery	8,500	9,427	*10.9%*
Piling machinery	2,964	3,752	*26.6%*
Earth moving machinery	1,250	1,501	*20.1%*
Other machinery	948	1,311	*38.3%*
Revenue (construction machinery)	**42,495**	**48,148**	***13.3%***
Other business	891	1,040	*16.7%*
Total revenue	**43,386**	**49,188**	***13.4%***
Gross margin			***Change (ppt)***
Concrete machinery	*29.6%*	*28.9%*	*(0.6)*
Excavator	*36.8%*	*34.9%*	*(2.0)*
Crane machinery	*25.8%*	*20.0%*	*(5.8)*
Piling machinery	*44.4%*	*43.6%*	*(0.9)*
Earth moving machinery	*36.5%*	*32.8%*	*(3.7)*
Other machinery	*31.2%*	*28.7%*	*(2.6)*
Gross margin (construction machinery)	***32.8%***	***30.7%***	***(2.1)***
Other business	*10.5%*	*12.1%*	*1.5*
Blended gross margin	***32.4%***	***30.3%***	***(2.0)***

Source: Company data, CMBIS

Figure 3: Quarterly results

	1Q19	1Q20	Change YoY	2Q19	2Q20	Change YoY
Total revenue	**21,295**	**17,266**	***-18.9%***	**22,092**	**31,921**	***44.5%***
Cost of sales	-14,754	-12,402	*-15.9%*	-14,594	-21,860	*49.8%*
Gross profit	**6,541**	**4,864**	***-25.6%***	**7,498**	**10,061**	***34.2%***
Other income	-87	-70	*-20.3%*	-129	-126	*-2.2%*
S&D expenses	-1,437	-942	*-34.5%*	-1,574	-1,604	*1.9%*
Administrative expenses	-992	-1,065	*7.5%*	-1,105	-1,517	*37.2%*
Fair value change	211	197	*-6.7%*	45	85	*89.5%*
Asset impairment	-160	-119	*-25.8%*	-315	-210	*-33.5%*
EBIT	**4,076**	**2,865**	***-29.7%***	**4,419**	**6,689**	***51.4%***
Net finance income/(expense)	-122	-312	*154.8%*	111	305	*174.2%*
Other gains/(losses)	-8	131	*n/a*	-242	467	*n/a*
Share of profit of JV and associates	31	-44	*n/a*	27	23	*-14.4%*
Pretax profit	**3,976**	**2,640**	***-33.6%***	**4,315**	**7,484**	***73.4%***
Income tax	-652	-426	*-34.6%*	-704	-1,060	*50.6%*
After tax profit	**3,325**	**2,214**	*-33.4%*	**3,611**	**6,425**	*77.9%*
MI	-104	-20	*-80.4%*	-84	-150	*78.5%*
Net profit	**3,221**	**2,194**	***-31.9%***	**3,527**	**6,274**	***77.9%***
Ratios:			*ppt*			*ppt*
Gross margin	*30.7%*	*28.2%*	*-2.5*	*33.9%*	*31.5%*	*-2.4*
S&D expense ratio	*6.7%*	*5.5%*	*-1.3*	*7.1%*	*5.0%*	*-2.1*
Administrative and R&D expense ratio	*4.7%*	*6.2%*	*1.5*	*5.0%*	*4.8%*	*-0.3*
Net profit margin	*15.6%*	*12.8%*	*-2.8*	*16.3%*	*20.1%*	*3.8*
Effective tax rate	*16.4%*	*16.1%*	*-0.2*	*16.3%*	*14.2%*	*-2.2*

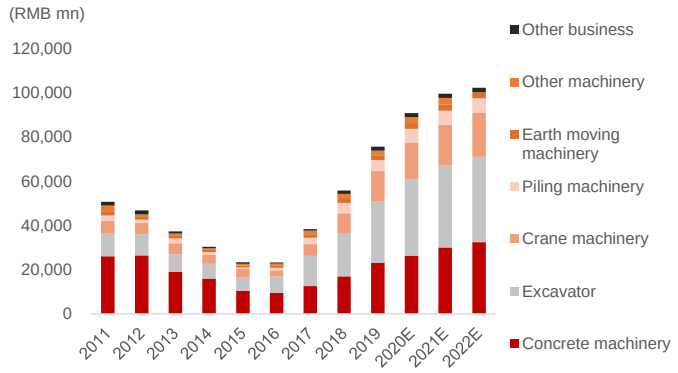
Source: Company data, CMBIS

Figure 4: Change in key assumptions

	Old			New			Change		
(RMB mn)	**2020E**	**2021E**	**2022E**	**2020E**	**2021E**	**2022E**	**2020E**	**2021E**	**2022E**
Revenue									
Concrete machinery	28,036	31,401	33,913	26,370	30,062	32,467	-5.9%	-4.3%	-4.3%
Excavator	35,462	37,944	39,462	34,691	37,119	38,604	-2.2%	-2.2%	-2.2%
Crane machinery	16,872	18,728	20,164	16,572	18,395	19,866	-1.8%	-1.8%	-1.5%
Piling machinery	5,277	5,540	5,707	6,107	6,413	6,605	15.7%	15.7%	15.7%
Earth moving machinery	2,262	2,375	2,446	2,594	2,724	2,805	14.7%	14.7%	14.7%
Other machinery	2,274	2,388	2,507	2,707	3,005	3,155	19.0%	25.9%	25.9%
Revenue (construction machinery)	**90,182**	**98,376**	**104,199**	**89,041**	**97,717**	**103,502**	-1.3%	-0.7%	-0.7%
Other business	1,827	1,918	2,014	1,827	1,918	2,014	0.0%	0.0%	0.0%
Total revenue	**92,009**	**100,294**	**106,213**	**90,868**	**99,635**	**105,517**	-1.2%	-0.7%	-0.7%
Revenue growth								ppt	
Concrete machinery	20.8%	12.0%	8.0%	13.7%	14.0%	8.0%	(7.2)	2.0	0.0
Excavator	28.4%	7.0%	4.0%	25.6%	7.0%	4.0%	(2.8)	(0.0)	0.0
Crane machinery	20.7%	11.0%	7.7%	18.5%	11.0%	8.0%	(2.1)	0.0	0.3
Piling machinery	9.7%	5.0%	3.0%	27.0%	5.0%	3.0%	17.3	(0.0)	0.0
Earth moving machinery	5.3%	5.0%	3.0%	20.8%	5.0%	3.0%	15.5	0.0	0.0
Other machinery	5.0%	5.0%	5.0%	25.0%	11.0%	5.0%	20.0	6.0	0.0
Revenue (construction machinery)	**22.0%**	**9.1%**	**5.9%**	**20.4%**	**9.7%**	**5.9%**	(1.5)	0.7	0.0
Other business	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	0.0	0.0	0.0
Total revenue	**21.6%**	**9.0%**	**5.9%**	**20.1%**	**9.6%**	**5.9%**	(1.5)	0.6	0.0
Gross margin								ppt	
Concrete machinery	32.0%	32.0%	31.0%	29.5%	31.5%	31.5%	(2.5)	(0.5)	0.5
Excavator	40.0%	39.0%	38.5%	38.0%	38.0%	38.0%	(2.0)	(1.0)	(0.5)
Crane machinery	25.7%	25.5%	25.5%	21.0%	23.0%	23.0%	(4.7)	(2.5)	(2.5)
Piling machinery	45.5%	45.0%	45.0%	45.5%	45.0%	45.0%	0.0	0.0	0.0
Earth moving machinery	36.5%	36.5%	36.5%	34.5%	36.5%	36.5%	(2.0)	0.0	0.0
Other machinery	30.0%	30.0%	30.0%	29.0%	30.0%	30.0%	(1.0)	0.0	0.0
Gross margin (construction machinery)	**34.8%**	**34.3%**	**33.6%**	**32.5%**	**33.3%**	**33.2%**	(2.4)	(0.9)	(0.4)
Other business	11.0%	11.0%	11.0%	12.0%	12.0%	12.0%	1.0	1.0	1.0
Blended gross margin	**34.3%**	**33.8%**	**33.2%**	**32.0%**	**32.9%**	**32.8%**	(2.3)	(0.9)	(0.4)
Net profit	**14,621**	**16,212**	**17,436**	**13,962**	**16,288**	**17,589**	**-4.5%**	**0.5%**	**0.9%**

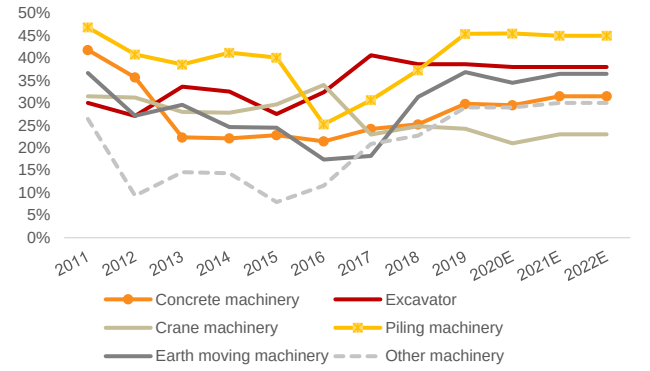
Source: Company data, CMBIS estimates

Figure 5: SANY revenue breakdown



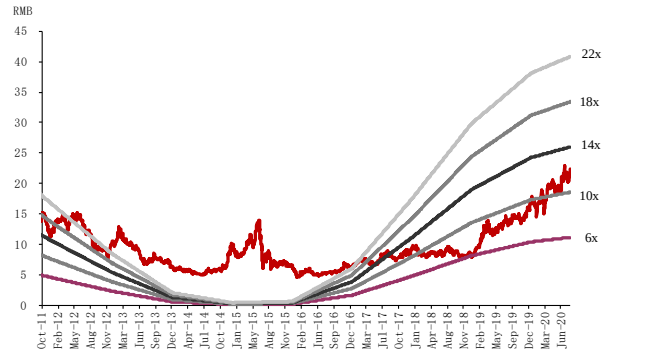
Source: Company data, CMBIS estimates

Figure 6: SANY gross margin trend



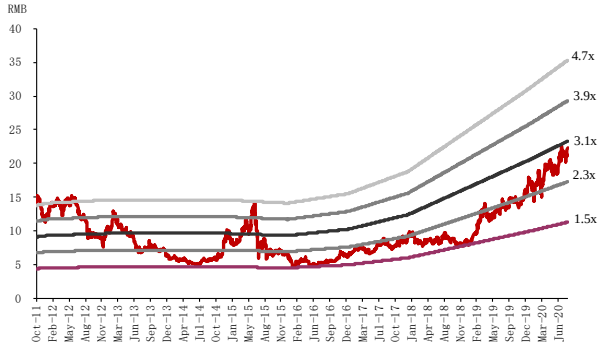
Source: Company data, CMBIS estimates

Figure 7: SANY's P/E band



Source: Company data, CMBIS estimates

Figure 8: SANY's P/B band



Source: Company data, CMBIS estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue	**55,822**	**75,666**	**90,868**	**99,635**	**105,517**
Cost of sales	(38,728)	(50,932)	(61,748)	(66,818)	(70,866)
Gross profit	**17,094**	**24,733**	**29,120**	**32,817**	**34,650**
Surcharge	(326)	(371)	(363)	(299)	(317)
S&D expenses	(4,447)	(5,488)	(5,725)	(6,177)	(6,542)
Administrative expenses	(3,800)	(5,696)	(6,815)	(6,974)	(7,281)
Fair value change	(362)	290	290	0	0
Asset impairment	(1,095)	(1,259)	(1,272)	(1,495)	(1,583)
EBIT	**7,063**	**12,209**	**15,234**	**17,872**	**18,928**
Net finance income/(cost)	(136)	46	369	791	1,312
Finance income	344	505	799	1,211	1,730
Finance expenses	(479)	(458)	(429)	(420)	(418)
Other gains/(losses)	495	1,059	800	600	600
Profit of JV and associates	128	140	202	200	177
Pretax profit	**7,550**	**13,454**	**16,605**	**19,462**	**21,017**
Income tax	(1,247)	(1,960)	(2,358)	(2,841)	(3,068)
After tax profit	**6,303**	**11,494**	**14,247**	**16,621**	**17,948**
MI	(187)	(288)	(285)	(332)	(359)
Net profit	**6,116**	**11,207**	**13,962**	**16,288**	**17,589**
D&A	1,932	2,020	2,031	2,048	2,063
EBITDA	**8,995**	**14,230**	**17,266**	**19,920**	**20,992**

Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Pretax profit	7,550	13,454	16,605	19,462	21,017
Finance cost	388	120	429	420	418
Interest income	(344)	(505)	(799)	(1,211)	(1,730)
Profit or loss of associates	(128)	(140)	(202)	(200)	(177)
Fair value change	(276)	(673)	0	0	0
Provision for assets	(8)	249	0	0	0
Depreciation and amortization	1,932	2,020	2,031	2,048	2,063
Income tax paid	(1,247)	(1,960)	(2,358)	(2,841)	(3,068)
Change in working capital	1,788	531	(2,220)	(2,461)	(99)
Others	870	167	0	0	0
Cash flow from operation	**10,527**	**13,265**	**13,487**	**15,218**	**18,424**
Net capex on PP&E	(1,003)	(2,157)	(1,500)	(1,500)	(1,500)
Investment in JV/associates	(648)	(11)	(50)	(50)	0
Investment in subsidiaries	311	153	0	0	0
Dividend received	13	14	20	20	0
Interest received	344	505	799	1,211	1,730
Others	(9,781)	(10,485)	(70)	0	0
Cash flow from investing	**(10,765)**	**(11,981)**	**(801)**	**(319)**	**230**
Equity financing/(repurchase)	0	0	0	0	0
Net bank borrowings	1,584	1,756	(300)	(200)	100
Dividend paid	(1,233)	(2,165)	(3,516)	(4,398)	(5,131)
Interest paid	(479)	(458)	(429)	(420)	(418)
Others	955	(283)	0	0	0
Cash flow from financing	**827**	**(1,151)**	**(4,245)**	**(5,018)**	**(5,449)**
Change in cash	589	134	8,441	9,880	13,205
Cash at beginning of the year	4,104	11,985	13,527	21,968	31,848
Exchange and others	7,293	1,408	0	0	0
Cash at the end of the year	11,985	13,527	21,968	31,848	45,053

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	**21,879**	**22,041**	**21,231**	**21,685**	**20,655**
PP&E	11,867	10,615	10,446	10,262	10,062
JV/associates	2,328	2,985	3,217	3,447	3,624
Goodwill	51	49	49	49	49
LT trade receivables	366	1,286	706	1,478	835
Intangible assets	3,880	3,339	3,048	2,683	2,319
AFS investments	1,121	0	0	0	0
Others	1,115	2,656	2,656	2,656	2,656
Deferred tax assets	1,152	1,109	1,109	1,109	1,109
Current assets	**51,896**	**68,500**	**85,506**	**95,116**	**113,285**
Inventories	11,595	14,252	16,199	17,118	17,830
Trade and bills receivables	20,802	21,793	28,993	26,693	31,703
Other receivables	1,704	3,030	2,447	3,559	2,801
Others	3,272	6,897	6,897	6,897	6,897
Cash	11,985	13,527	21,968	31,848	45,053
Current liabilities	**33,935**	**42,149**	**47,913**	**46,055**	**50,375**
Trade and bills payables	17,191	20,295	26,059	24,101	28,321
Bank borrowings	8,336	10,771	10,771	10,871	10,971
Tax payable	524	1,490	1,490	1,490	1,490
Others	3,567	4,162	4,162	4,162	4,162
Non-current liabilities	**7,337**	**2,866**	**2,566**	**2,266**	**2,266**
Bank borrowings	5,974	1,303	1,003	703	703
Deferred tax liabilities	650	714	714	714	714
Others	471	728	728	728	728
Equity	**32,502**	**45,527**	**56,258**	**68,481**	**81,298**
Shareholders' equity	31,485	44,421	54,868	66,758	79,216
MI	1,017	1,106	1,391	1,723	2,082

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Concrete machinery	30%	31%	29%	30%	31%
Excavator	34%	37%	38%	37%	37%
Crane machinery	17%	18%	18%	18%	19%
Piling machinery	8%	6%	7%	6%	6%
Earth moving machinery	4%	3%	3%	3%	3%
Other machinery	4%	3%	3%	3%	3%
Other business	3%	2%	2%	2%	2%
Total	100%	100%	100%	100%	100%
Profit & loss ratio (%)					
Gross margin	30.6	32.7	32.0	32.9	32.8
EBIT margin	12.7	16.1	16.8	17.9	17.9
Net profit margin	11.3	15.2	15.7	16.7	17.0
Growth (%)					
Revenue	45.6	35.5	20.1	9.6	5.9
Gross profit	48.3	44.7	17.7	12.7	5.6
EBIT	n/a	72.9	24.8	17.3	5.9
Net profit	192.3	83.2	24.6	16.7	8.0
Balance sheet ratio					
Current ratio (x)	1.5	1.6	1.8	2.1	2.2
Receivable turnover days	133	107	106	106	105
Inventory turnover days	91	93	90	91	90
Payable turnover days	133	134	137	137	135
Net debt / total equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Profitability (%)					
ROA	9.3	13.6	14.2	14.6	14.0
ROE	21.5	29.5	28.1	26.8	24.1
Per share data					
EPS (RMB)	0.79	1.36	1.65	1.92	2.08
BVPS (RMB)	4.04	5.27	6.48	7.89	9.36
DPS (RMB)	0.28	0.43	0.52	0.61	0.65

Source: Company data, CMBIS estimates

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