

ChinaSoft Int'l (354 HK)

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Company Update

BUY

UNCHANGED

Close price: HK\$4.10

Target Price: HK\$6.00 (+46%)

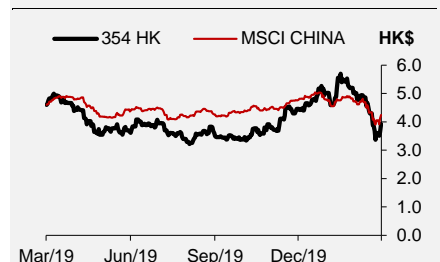
Prior TP: HK\$5.50

Key Data

HKEx code	354
12 Months High (HK\$)	5.80
12 Month Low (HK\$)	3.19
3M Avg Dail Vol. (mn)	26.02
Issue Share (mn)	2,624.71
Market Cap (HK\$mn)	10,761.30
Fiscal Year	12/2019
Major shareholder (s)	Dr. Chen Yu Hong (10.46%)

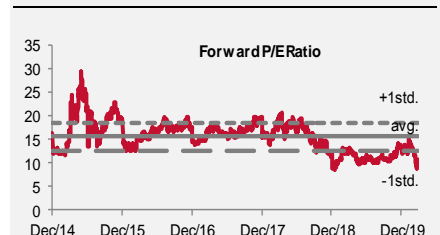
Source: Company data, Bloomberg, OP Research
Closing price are as of 26/03/2020

Price Chart



	1mth	3mth	6mth
Absolute %	-18.8	-7.2	18.5
Rel. MSCI CHINA %	-8.5	4.6	17.4

PE



Company Profile

ChinaSoft is a global leading IT outsourcing and solution service company

Cloud business ready to accelerate in FY20E

- CSI reported 13.8%/5.5% yoy growth in FY19 revenue/net earnings to RMB12,042mn/RMB755mn respectively, in line with our expectations. FY20E outlook turns more positive with accelerating cloud business.
- We revise up our FY20/21E core earnings estimate by 3.7%/11.5% to RMB951mn/RMB1,154mn respectively.
- Maintain BUY with new TP HK\$6.00 based on same 16x FY20E P/E, beneficiary of Huawei's raised R&D budget and New Infrastructure initiatives.

FY20E outlook turning more positive. Chinasoft (CSI) reported solid set of FY19 results with revenue up 13.8% to RMB12,042mn, of which revenue from TPG/IIG segment each contributed RMB10,458mn/RMB1,584mn respectively, representing 14.0%/12.3% yoy growth. CSI has seen steady growth from existing large customers (Huawei, HSBC, BAT and Ping'an) during the year, especially in the services from Cloud Intelligent Group. **GPM** edged down 0.9ppts to 29.8% from 30.7% in FY18 mainly due to the personnel redundancy in Huawei business line during the restricted list incident. We expect GPM to recover in FY19 as the company exercises more flexible human resources mgmt. **SG&A ratio** remained largely stable as improved operation efficiency mitigated increased sales & promotion outgoings. As a result, FY19 net earnings increased by 5.5% yoy to RMB755mn, up to OP expectations. The board recommended a final dividend of HK\$2.19cents per share (vs HK\$2.15cents in FY18), representing 7.6% payout.

We spotted a **more positive** tone from the mgmt when commenting on FY20E outlook. Expected growth drivers include (1) accelerated development in Cloud Intelligent Segment with closer cooperation with Huawei and other large clients, (2) New Infrastructure orders from local governments, and (3) upgraded Joint Force platform. The Chairman targets RMB30bn revenue by 2023E, implying 4-year CAGR of over 25%.

We revise up our FY20/21E core earnings estimates by 3.7%/11.5% to RMB951mn/RMB1,154mn. We revise up our FY20/21E revenue estimate by 5.7%/9.4% to RMB13,879mn/RMB15,498mn as we expect faster ramp-up of cloud intelligent business. Meanwhile, we tune up our FY20/21E GPM by 0.8ppts/0.8ppts to 30.7%/30.7%. As a result, our FY20/21E diluted EPS is revised up by 9.7%/18.0% to HK\$0.377/HK\$0.457 respectively.

Maintain BUY. Revise up our TP to HK\$6.00 based on same 16x FY20x P/E. Huawei announced to raise its 2020E R&D budget by 40% to US\$20bn on 25 March. We see CSI as a key beneficiary of Huawei's raised R&D budget and the New Infrastructure initiatives.

Risks: (1) slower than expected revenue growth in cloud services; (2) higher than expected staff costs; (3) high customer concentration.

Exhibit 1: Forecast and Valuation

Year to Dec (RMB mn)	FY18	FY19	FY20E	FY21E	FY22E
Revenue	10,585	12,042	13,879	15,498	17,296
Growth (%)	15	14	15	12	12
Adj. Net Profit	769	765	951	1,154	1,381
Growth (%)	7	(0)	24	21	20
Diluted Adj EPS (HK\$)	0.332	0.330	0.377	0.457	0.547
Adj EPS growth (%)	1	(1)	14	21	20
Change to previous EPS (%)			9.7	18.0	
Consensus EPS (HK\$)			0.399	0.478	
ROE (%)	13.8	12.3	13.7	14.6	15.2
P/E (x)	12.4	12.4	10.9	9.0	7.5
P/B (x)	1.4	1.4	1.3	1.1	1.0
Yield (%)	0.6	0.6	0.7	0.9	1.0
DPS (HK\$)	0.026	0.025	0.029	0.035	0.042

Source: Bloomberg, OP Research

Exhibit 2: Earnings revision

(RMB mn)	FY20E			FY21E			OP Comment
	New	Old	% Chg	New	Old	% Chg	
Revenue	13,879	13,125	5.7	15,498	14,161	9.4	As we expect acceleration in Cloud Intelligent business development
Gross profit	4,260	3,929	8.4	4,757	4,239	12.2	
Gross margin	30.7%	29.9%	0.8	30.7%	29.9%	0.8	Expect moderate margin recovery
Opex	(3,101)	(2,785)	11.3	(3,383)	(2,968)	14.0	
EBIT	1,218	1,213	0.4	1,434	1,344	6.7	
EBIT Margin	8.8%	9.2%	(0.5)	9.3%	9.5%	(0.2)	
Adj. Net Profit	951	918	3.7	1,154	1,035	11.5	
Diluted EPS (HK\$)	0.377	0.343	9.7	0.457	0.387	18.0	Due to lapsed share option

Source: OP Research

Exhibit 3: FY19 results review

RMB mn	1H18	2H18	1H19	2H19A	2H19E	Act./Est.(%)	OP Comments	FY18	FY19	yoy%
Revenue	4,814	5,771	5,538	6,504	6,341	2.6%		10,585	12,042	13.8%
COGS	(3,424)	(3,917)	(3,971)	(4,487)	(4,357)	3.0%		(7,340)	(8,459)	15.2%
Gross profit	1,390	1,855	1,567	2,016	1,985	1.6%		3,245	3,583	10.4%
Other income & gains	23	36	60	78	2	4726.3%	Due to the VAT input tax deduction	58	138	136.9%
Selling exp	(233)	(263)	(266)	(352)	(297)	18.5%		(496)	(618)	24.6%
Admin exp	(680)	(411)	(833)	(363)	(376)	-3.5%		(1,091)	(1,196)	9.6%
R&D	0	(739)	0	(809)	(778)	3.9%		(739)	(809)	9.4%
Other opex	(37)	(32)	(42)	(16)	(34)	-52.0%		(68)	(59)	-13.8%
Finance costs	(59)	(66)	(88)	(78)	(82)	-4.8%		(125)	(166)	32.7%
Profit after financing costs	404	380	398	476	419	13.6%		783	874	11.6%
Associated cos	(15)	27	(8)	8	8	-4.2%		12	(0)	-102.7%
Provision for other items	0	(35)	0	(75)	0	n.a.		(35)	(75)	112.5%
Pre-tax profit	388	372	390	409	427	-4.2%		760	799	5.1%
Tax	(33)	(12)	(31)	(11)	(50)	-78.1%		(44)	(42)	-4.5%
Minority interests	3	(3)	4	(6)	(7)	-25.4%		(0)	(2)	388.6%
Adj. Net profit	385	384	369	396	373	6.3%		769	765	-0.5%
Reported Net profit	359	357	363	392	369	6.3%		716	755*	5.5%
Key ratios						(in ppts)				(in ppts)
GPM	28.9%	32.1%	28.3%	31.0%	31.3%	(0.30)		30.7%	29.8%	(0.90)
S&G / sales	4.8%	4.5%	4.8%	5.4%	4.7%	0.73		4.7%	5.1%	0.45
Admin / sales	14.1%	7.1%	15.0%	5.6%	5.9%	(0.35)		10.3%	9.9%	(0.38)
EIT	8.4%	3.1%	8.0%	2.7%	11.8%	(9.12)		5.8%	5.3%	(0.53)
Adj. net margin	8.0%	6.7%	6.7%	6.1%	5.9%	0.21		6.8%	6.3%	(0.49)
% YoY										
Revenue	16%	13%	15%	13%	10%			15%	14%	
Gross profit	22%	15%	13%	9%	7%			18%	10%	
Adj. Net profit	21%	-4%	-4%	3%	-3%			27%	5%	

*We estimate RMB10mn share-based compensation for FY19.

Source: Company, OP Research

Financial Summary

Year to Dec	FY18	FY19	FY20E	FY21E	FY22E
Income Statement (RMB mn)					
TPG	9,022	10,215	11,850	13,272	14,864
ITG	1,317	1,422	1,564	1,704	1,858
Sales of hardware	246	405	466	522	574
Turnover	10,585	12,042	13,879	15,498	17,296
YoY%	15	14	15	12	12
COGS	(7,340)	(8,459)	(9,619)	(10,741)	(11,987)
Gross profit	3,245	3,583	4,260	4,757	5,309
Gross margin	30.7%	29.8%	30.7%	30.7%	30.7%
Other income	58	138	59	61	64
Selling & distribution	(496)	(618)	(695)	(764)	(840)
Admin	(1,091)	(1,196)	(1,399)	(1,504)	(1,622)
R&D	(739)	(809)	(924)	(1,022)	(1,131)
Other opex	(68)	(59)	(83)	(93)	(104)
Total opex	(2,395)	(2,681)	(3,101)	(3,383)	(3,697)
Operating profit (EBIT)	909	1,040	1,218	1,434	1,676
Operating margin	8.6%	8.6%	8.8%	9.3%	9.7%
Provisions	(35)	(75)	(50)	(50)	(50)
Finance costs	(125)	(166)	(156)	(156)	(156)
Profit after financing costs	748	799	1,012	1,228	1,469
Associated companies & JVs	12	(0)	(0)	(0)	(0)
Pre-tax profit	760	799	1,012	1,227	1,469
Tax	(44)	(42)	(56)	(68)	(81)
Minority interests	(0)	(2)	(5)	(6)	(7)
Adj. Net profit	769	765	951	1,154	1,381
YoY%	7	(0)	24	21	20
Net margin	7.3%	6.4%	6.9%	7.4%	8.0%
Reported Net profit	716	755	951	1,154	1,381
EBITDA	1,088	1,148	1,315	1,518	1,750
EBITDA margin	10.3%	9.5%	9.5%	9.8%	10.1%
EPS (RMB)	0.277	0.287	0.327	0.397	0.475
YoY%	1	4	14	21	20
DPS (HK\$)	0.026	0.025	0.029	0.035	0.042
Cash Flow (RMB mn)					
EBITDA	1,088	1,148	1,315	1,518	1,750
Chg in working cap	(894)	(413)	(339)	(285)	(317)
Others	49	234	(50)	(50)	(50)
Operating cash	243	969	925	1,183	1,383
Tax	(82)	(125)	(84)	(56)	(68)
Net cash from operations	161	844	841	1,127	1,316
Capex	(151)	(171)	(197)	(220)	(246)
Investments	(37)	(42)	(49)	(54)	(61)
Dividends received	1	0	0	0	0
Sales of assets	9	0	0	0	0
Interests received	12	12	12	14	17
Others	(2)	0	0	0	0
Investing cash	(167)	(201)	(234)	(261)	(290)
FCF	(6)	643	607	866	1,026
Issue of shares	109	0	0	0	0
Buy-back	(76)	0	0	0	0
Minority interests	0	0	0	0	0
Dividends paid	(37)	(37)	(48)	(66)	(80)
Net change in bank loans	984	(9)	0	0	0
Interests paid	(85)	(166)	(156)	(156)	(156)
Others	(41)	123	0	0	0
Financing cash	853	(89)	(204)	(222)	(236)
Net change in cash	847	554	403	644	790
Exchange rate or other Adj	14	(675)	0	0	0
Opening cash	1,785	2,646	2,526	2,929	3,573
Closing cash	2,646	2,526	2,929	3,573	4,363
CFPS (HK\$)					

Source: Company, OP Research

Year to Dec	FY18	FY19	FY20E	FY21E	FY22E
Ratios					
Gross margin (%)	30.7	29.8	30.7	30.7	30.7
Operating margin (%)	8.6	8.6	8.8	9.3	9.7
Adj. Net margin (%)	7.3	6.4	6.9	7.4	8.0
Selling & dist'n exp/Sales (%)	4.7	5.1	5.0	4.9	4.9
Admin exp/Sales (%)	10.3	9.9	10.1	9.7	9.4
R&D exp/Sales (%)	7.0	6.7	6.7	6.6	6.5
Payout ratio (%)	7.8	7.6	7.6	7.6	7.6
Effective tax (%)	5.9	5.3	5.5	5.5	5.5
Total debt/equity (%)	43.8	40.3	35.3	30.8	26.7
Net debt/equity (%)	Net cash	1.2	Net cash	Net cash	Net cash
Current ratio (x)	2.26	2.68	2.84	3.02	3.22
Quick ratio (x)	2.25	2.66	2.82	3.00	3.20
Inventory T/O (days)	3	2	2	2	2
AR T/O (days)	90	100	100	100	100
AP T/O (days)	74	53	53	53	53
Cash conversion cycle (days)	19	49	49	49	49
Asset turnover (x)	1.11	1.15	1.25	1.26	1.26
Financial leverage (x)	1.71	1.68	1.61	1.55	1.50
EBIT margin (%)	8.6	8.6	8.8	9.3	9.7
Interest burden (x)	0.84	0.77	0.83	0.86	0.88
Tax burden (x)	1.01	0.96	0.94	0.94	0.94
Return on equity (%)	13.8	12.3	13.7	14.6	15.2
ROIC (%)	15.4	15.7	16.8	18.5	20.3
Balance Sheet (RMB mn)					
Fixed assets	838	802	927	1,076	1,250
Intangible assets & goodwill	1,155	1,101	1,114	1,143	1,185
Associated companies & JVs	144	228	227	227	227
Long-term investments	0	0	0	0	0
Other non-current assets	127	416	416	416	416
Non-current assets	2,264	2,547	2,685	2,862	3,077
Inventories	64	54	62	69	77
AR	2,607	3,302	3,805	4,249	4,742
Prepayments & deposits	1	0	0	0	0
Other current assets	2,740	2,178	2,178	2,178	2,178
Cash	2,646	2,526	2,929	3,573	4,363
Current assets	8,059	8,060	8,974	10,069	11,360
AP	1,497	1,229	1,398	1,561	1,742
Tax	125	84	56	68	81
Accruals & other payables	45	22	25	28	32
Bank loans & leases	1,676	1,649	1,649	1,649	1,649
CB & other debts	216	27	27	27	27
Other current liabilities	0	0	0	0	0
Current liabilities	3,560	3,011	3,155	3,333	3,530
Bank loans & leases	0	200	200	200	200
CB & other debts	720	728	728	728	728
Deferred tax & others	11	134	134	134	134
MI	65	66	71	77	84
Non-current liabilities	796	1,128	1,133	1,139	1,146
Total net assets	5,967	6,468	7,371	8,459	9,761
Shareholder's equity	5,967	6,468	7,371	8,459	9,761
Share capital	113	116	116	116	116
Reserves	5,854	6,351	7,254	8,343	9,645
BVPS (HK\$)	2.90	2.92	3.23	3.71	4.28
Total debts	2,612	2,603	2,603	2,603	2,603
Net cash/(debts)	34	(78)	325	969	1,759

Exhibit 4: Peer Group Comparison

Company	Ticker	Price	Mkt	3-mth	PER	EPS			EPS	P/B				P/B	EV/	EV/	Net	Gross	Net					Sh px	
			cap	avg t/o	Hist	PER	PER	FY1	FY2	3-Yr	EPS	PEG	Div yld	Div yld	Hist	FY1	Ebitda	Ebitda	gearing	margin	margin	ROE	ROE	Sh px	3-mth
			(US\$m)	(US\$m)	(x)	FY1 (x)	FY2 (x)	YoY%	YoY%	Cagr (%)	(x)	Hist (%)	FY1 (%)	(x)	(x)	Hist	Cur Yr	Hist (%)	Hist (%)	Hist (%)	Hist (%)	FY1 (%)	1-mth %	%	
Chinasoft Intl	354 HK	4.10	1,388	15.9	12.4	10.9	9.0	14.1	21.3	18.3	0.59	0.6	0.7	1.40	1.27	9.2	7.9	1.2	29.8	6.3	12.3	13.7	(17.7)	(8.1)	
HSI		23,352.34			9.5	9.5	8.6	0.3	10.4	4.8	1.96	4.3	4.5	1.00	0.94						10.5	9.9	(12.5)	(16.2)	
HSCEI		9,447.56			7.6	7.6	6.9	(0.5)	10.3	3.6	2.10	4.0	4.3	0.98	0.93						13.0	12.2	(10.0)	(14.4)	
CSI300		3,698.05			13.2	10.9	9.7	20.7	12.9	2.4	4.53	2.2	2.8	1.68	1.47						12.7	13.5	(9.2)	(8.1)	
Adjusted sector avg*					30.1	40.7	21.3	13.8	9.4	11.6	1.69	1.9	2.1	3.17	4.10	9.0	8.4	0.0	34.6	15.8	13.6	16.7	(18.3)	(16.2)	
Infosys Ltd	INFO IN	634.00	35,844	87.3	17.9	16.2	14.8	10.1	9.4	9.6	1.70	2.9	3.7	4.42	4.28	12.2	11.3	0.0	34.8	18.6	26.0	25.8	(19.0)	(13.0)	
Tata Consultancy	TCS IN	1,774.95	88,383	94.5	21.4	20.4	18.9	4.9	8.1	7.5	2.71	3.8	3.8	7.82	7.15	16.1	15.1	0.0	41.9	21.5	38.0	35.3	(16.4)	(19.4)	
Cognizant Tech-A	CTSH US	47.69	26,165	251.7	14.5	11.8	10.9	22.1	8.7	13.4	0.88	1.7	2.1	2.37	2.09	7.6	7.5	0.0	36.6	11.0	16.4	18.9	(24.6)	(23.2)	
Wipro Ltd-Adr	WIT US	2.79	15,940	3.7	N/A	12.3	12.1	N/A	1.3	N/A	N/A	0.5	0.5	N/A	N/A	8.3	7.6	0.0	29.5	15.4	18.2	16.9	(23.4)	(26.6)	
Travelsky Tech-H	696 HK	14.26	5,381	9.5	16.5	15.0	14.4	9.9	4.1	10.2	1.47	2.1	2.2	2.16	2.03	9.9	8.7	0.0	N/A	31.1	14.3	13.9	(13.6)	(24.6)	
Kingdee Intl Sft	268 HK	10.10	4,331	26.6	80.2	96.3	77.0	(16.7)	25.0	17.3	5.56	0.1	0.1	5.13	4.94	31.7	39.6	0.0	80.4	11.2	6.5	4.9	0.4	24.7	
Neusoft Corp-A	600718 CH	12.41	2,173	42.3	137.9	112.8	56.4	22.2	100.0	N/A	N/A	N/A	N/A	1.77	N/A			0.0	30.0	1.5	0.2	1.2	(12.9)	9.5	

* Outliners and "N/A" entries are in red and excl. from the calculation of averages

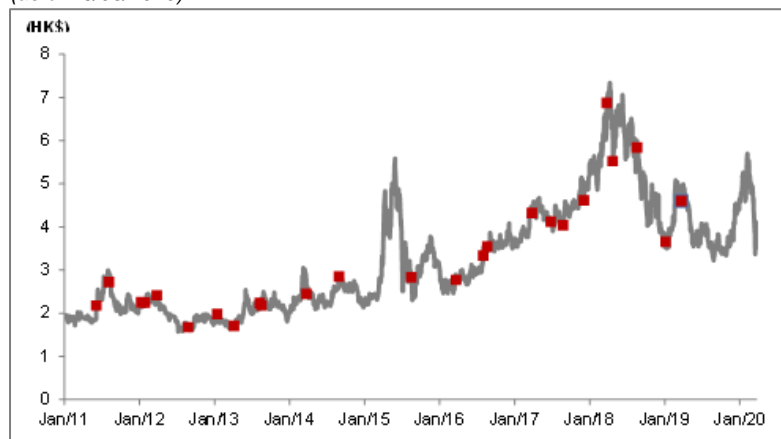
Source: Bloomberg, OP Research

Our recent reports

Date	Company / Sector	Code	Title	Rating	Analyst
25/03/2020	Anta Sports	2020	FY20E strive for positive growth	BUY	Dallas Cai/Megan Jin
25/03/2020	China Overseas PPT	2669	FY19 results up to expectations	HOLD	Dallas Cai
23/03/2020	CG Services	6098	FY19 saw solid set of results	BUY	Dallas Cai
20/03/2020	Kingdee Int'l	268	Ambitious cloud target to weigh on FY20E earnings	HOLD	Dallas Cai
20/03/2020	Xtep Intl	1368	FY19 results in line with expectations	BUY	Dallas Cai/Megan Jin
19/03/2020	A-Living	3319	Unfolding a new 3-year plan	BUY	Dallas Cai
19/03/2020	Ausnutria Dairy	1717	Robust growth momentum to keep up in FY20E	BUY	Dallas Cai/Megan Jin
19/03/2020	361 Degrees Intl	1361	FY19 results up to expectations	BUY	Megan Jin
18/03/2020	Sunny Optical	2382	FY19 results clean beat on GPM	BUY	Dallas Cai
10/03/2020	Q Tech	1478	FY19 results beat on better CCM product mix	BUY	Dallas Cai
09/03/2020	Edvantage Group	382	1H20/21E positive profit alert - BUY	BUY	Dallas Cai/Megan Jin
24/02/2020	361 Degrees Intl	1361	COVID-19 impact to be inevitable on 1H20E	BUY	Megan Jin
20/02/2020	Ausnutria Dairy	1717	FY19E cow IMF growth beat expectations	BUY	Dallas Cai/Megan Jin
18/02/2020	Anta Sports	2020	Concrete yet manageable impacts from COVID-19	BUY	Dallas Cai/Megan Jin
13/02/2020	CH Display OPT	334	Better than feared coronavirus impacts, for now	HOLD	Dallas Cai
10/02/2020	TCL Electronics	1070	FY19E earnings beat expectations	BUY	Dallas Cai
05/02/2020	Xtep Intl	1368	4Q19 in line with expectations	BUY	Dallas Cai/Megan Jin
17/01/2020	Edvantage Group	382	FY20/21E saw a good start	BUY	Yuji Fung/Dallas Cai
17/01/2020	361 Degrees Intl	1361	4Q19 retail sales on track	BUY	Megan Jin
15/01/2020	Anta Sports	2020	Issuance of CB to optimize financial structure	BUY	Dallas Cai/Megan Jin
10/01/2020	Sunny Optical	2382	2019 shipment targets met - as expected	BUY	Yuji Fung/Dallas Cai
08/01/2020	Q Tech	1478	2019 full year shipments meet OP targets	BUY	Yuji Fung/Dallas Cai
31/12/2019	GT Service	2869	Introducing Longfor as 3rd largest shareholder	BUY	Dallas Cai/Yuji Fung
20/12/2019	Q Tech	1478	Top-up placement for CCM capacity expansion	BUY	Yuji Fung/Dallas Cai
17/12/2019	Aidigong	286	Transforming into a leading postpartum care player in China	NR	Yuji Fung
13/12/2019	Anta Sports	2020	Revealing higher visibility of post-M&A roadmap	BUY	Dallas Cai/Megan Jin
10/12/2019	Sunny Optical	2382	November saw strong HCM shipment growth	BUY	Yuji Fung/Dallas Cai

Historical recommendations and target price: Chinasoft Intl (354 HK)

(as of 26/03/2020)



DATE	RATING	TP (HK\$)	CLOSE (HK\$)	DATE	RATING	TP (HK\$)	CLOSE (HK\$)
1 28 Mar 2014	HOLD	2.70	2.46	9 28 Aug 2017	BUY	6.30	4.07
2 02 Sep 2014	HOLD	3.40	2.87	10 07 Dec 2017	BUY	7.50	4.65
3 20 Aug 2015	BUY	3.30	2.85	11 28 Mar 2018	BUY	8.80	6.93
4 24 Mar 2016	HOLD	3.04	2.79	12 26 Apr 2018	BUY	8.80	5.57
5 04 Aug 2016	HOLD	4.50	3.36	13 23 Aug 2018	BUY	8.50	5.87
6 24 Aug 2016	BUY	5.80	3.57	14 08 Jan 2019	BUY	6.23	3.55
7 29 Mar 2017	BUY	6.67	4.36	15 22 Mar 2019	BUY	6.14	4.68
8 28 Jun 2017	BUY	6.20	4.15	16 21 Aug 2019	BUY	5.50	3.60

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