

# AAC Technologies Holdings

Bloomberg: 2018 HK Equity | Reuters: 2018.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

16 May 2022

## BUY

Last Traded Price (13 May 2022): HK\$16.26 (HSI : 19,899)  
Price Target 12-mth: HK\$22.30 (37% upside) (Prev HK\$24.70)

### Analyst

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### What's New

- 1Q22 revenue was Rmb4.9bn, up 14% y-o-y, driven by better-than-expected optics and acoustics revenue growth
- Net profit decreased 62% y-o-y, missing the market consensus, mainly dragged by ASP pressure
- Cut FY22/23/24F net profit by 10%/14%/22% to mainly reflect Optics's margin cut
- Maintain BUY, TP lowered to HK\$22.30; impact from slowing profit growth already in the price

### Price Relative



### Forecasts and Valuation

FY Dec (RMBm)	2021A	2022F	2023F	2024F
Turnover	17,667	20,432	23,355	28,166
EBITDA	4,521	4,754	5,105	5,599
Pre-tax Profit	1,413	1,451	1,519	1,617
Net Profit	1,316	1,300	1,362	1,428
Net Pft (Pre Ex) (core profit)	1,315	1,242	1,297	1,349
Net Profit Gth (Pre-ex) (%)	(3.2)	(5.5)	4.4	4.1
EPS (RMB)	1.09	1.08	1.13	1.18
EPS (HK\$)	1.26	1.25	1.31	1.37
Core EPS (RMB)	1.09	1.03	1.07	1.12
Core EPS (HK\$)	1.26	1.19	1.24	1.29
EPS Gth (%)	(12.5)	(1.2)	4.8	4.9
Core EPS Gth (%)	(3.0)	(5.5)	4.4	4.1
Diluted EPS (HK\$)	1.26	1.25	1.31	1.39
DPS (HK\$)	0.39	0.38	0.40	0.43
BV Per Share (HK\$)	20.90	21.88	22.85	23.88
PE (X)	12.9	13.1	12.5	11.9
CorePE (X)	12.9	13.7	13.1	12.6
P/Cash Flow (X)	7.7	3.7	5.0	4.0
P/Free CF (X)	nm	nm	nm	nm
EV/EBITDA (X)	4.7	4.7	4.9	5.0
Net Div Yield (%)	2.4	2.3	2.5	2.6
P/Book Value (X)	0.8	0.7	0.7	0.7
Net Debt/Equity (X)	0.2	0.2	0.3	0.4
ROAE (%)	6.1	5.8	5.8	5.9
Earnings Rev (%)		(10)	(14)	(22)
Consensus EPS (RMB)		1.03	1.32	1.62
Other Broker Recs:		B:16	S:5	H:16

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

## Optics growth maintained

### Investment Thesis

The expectation of strong optics performance is driven by 1) optimisation of the product mix due to increased revenue share from high-end products, 2) an increasing market share, and 3) vertical expansion of products including CCM and vehicle modules. AAC Technology (AAC)'s optics revenue is expected to maintain robust growth at a CAGR of 60.2% for FY21-24F, accounting for 25%/35% of revenue in FY23/24.

Seizing opportunities in the IoT market and the spec upgrade trend in true wireless stereo earphones and notebooks. The microelectromechanical systems (MEMS) segment is to be the second fastest growing business with ample room for growth and is expected to grow at a CAGR of 16% in FY21-24F.

Potential spin-off and separate listing of AAC Optics helps drive the valuation of its optics business to its peers' level.

### Valuation:

Our TP has been lowered to HK\$22.30, as we have toned down FY22F EPS, still pegged to an unchanged target PE of 17x FY22F, based on its strong optics business growth.

### Where we differ:

Our revenue forecast in the optics segment is higher than the market consensus by 7%/6%/24% in FY22/23/24F, owing to the market share increase and the optimisation of the product mix by increasing high-end component.

### Key Risks to Our View:

1) Sluggish growth in global smartphone shipment persisting due to deteriorating consumer sentiment and 2) further loss of market share in the handset dynamic component space due to rigorous competition.

### At A Glance

Issued Capital (m shrs)	1,208
Mkt Cap (HKm/US\$m)	19,642 / 2,502
Major Shareholders (%)	
Wu (Chunyuan Ingrid)	21.8
Pan (Zhengmin Benjamin)	19.4
Free Float (%)	58.8
3m Avg. Daily Val. (US\$m)	21.97
GICS Industry: Information Technology / Technology	
Hardware & Equipment	



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## AAC Technologies Holdings

### WHAT'S NEW

#### 1Q earnings missed expectations, margin improvement expected in 2H22

##### 1Q22 result highlights

**Revenue ahead of market expectations.** Revenue was Rmb4.9bn, up 14.1% y-o-y, beating the market consensus by 12.7%. The growth was mainly attributable to the above market expectation optics revenue growth and the growth in demand from key customers in the acoustics segment. Optics and precision mechanics grew 36.4% y-o-y and 22.2% y-o-y, respectively, by market share gain. Meanwhile, the acoustics segment increased slightly by 6.4% y-o-y.

**Gross margin contracted to 19.5%, down 8.2ppt y-o-y,** due to margin contractions in all segments under fierce competition and a higher contribution from the low-margin optics business. The optics segment margin increased 5.6ppt to 3.5% q-o-q but was down 24.0ppt y-o-y because of ASP pressure from key customers and low utilization (c.50 to 60%) of production capacity due to destocking. It may take one to two more months to reach its optimum inventory level of two to three months and for the utilization rate to ramp up.

**1Q22 net profit decreased by 61.5% y-o-y to Rmb205.3m,** missing the market consensus, mainly dragged by the gross margin contraction.

##### Our view

We still expect optics to be the main growth driver in the coming three years, on the back of increasing penetration among overseas clients and mass production of new products like wafer level glass (WLG) hybrid lenses. Its revenue growth remains intact, at 60.2% in FY21-24F.

However, we expect the margin contraction, especially in the optics business, to be maintained in 2Q. Nevertheless, it should start easing in 2H22 due to a utilisation rate ramp-up after destocking and increased penetration for

high-end products, like modules for mid to high-end phones and WLG hybrid lenses.

As the company has been optimising its R&D expenses, we expect the decrease in earnings due to margin contraction to be partially offset by the cost savings from the reduction in research expenses.

We lower our gross margin assumption for optics segment by 9.5/7.4/7.0ppt to 12.0%/14.1%/14.5%, in FY22/23/24F and thus cut our earnings by 9.6%/13.5%/21.8% for FY22/23/24F respectively.

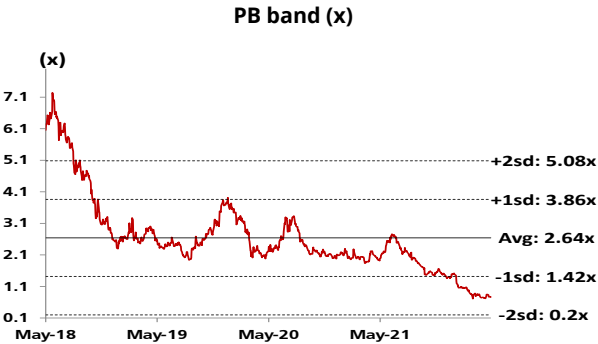
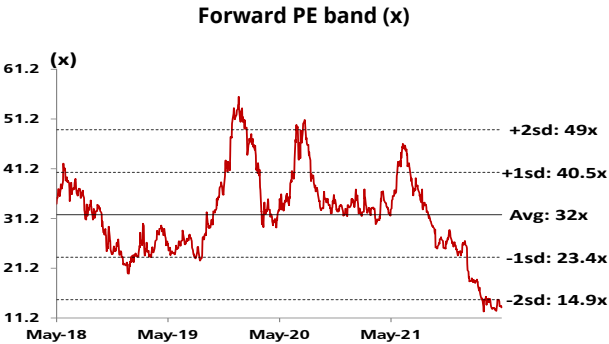
We lower our TP to HK\$22.3. AAC is trading at a 12.2x FY22F PE, below its five-year average forward PE of 17.0x. We expect the negatives to be already priced in and maintain BUY.

##### Company Background

AAC Technologies (AAC) is the world's leading smartphone component supplier. It was established in 1993 and listed on the HKEx in 2005. It has a 20%-30% market share in the acoustics and haptics segments. The company has demonstrated its ability to expand into new verticals, moving from (1) acoustics (i.e., speakers and receivers) to (2) electromagnetic drives & precision mechanics (i.e., haptics and radio frequency [RF] mechanical) to (3) optics, and (4) MEMS, which accounted for 49%, 32%, and 14% of its FY21 revenue, respectively. Benjamin Pan, the chief executive officer, is the founder and largest shareholder of the company.

**AAC Technologies Holdings**

**Historical PE and PB band**



Source: Thomson Reuters, DBS HK

## AAC Technologies Holdings

### Key Assumptions

FY Dec	2020A	2021A	2022F	2023F	2024F
Acoustics Business revenue	7,560.0	8,582.1	9,207.1	9,271.5	9,336.4
Gross Margin (%)	27.9	29.7	28.7	28.7	29.0
Optics products revenue	1,634.4	2,389.4	3,777.0	5,802.6	9,831.0
Gross Margin (%)	0.0	17.2	13.5	16.5	18.0

Source: Company, DBS HK

### Segmental Breakdown (RMB m)

FY Dec	2020A	2021A	2022F	2023F	2024F
<b>Revenues (RMB m)</b>					
Dynamic components	7,560	8,582	9,207	9,272	9,336
Electromagnetic drives and precision mechanics	6,847	5,639	6,218	6,917	7,387
Optics products	1,634	2,389	3,777	5,803	9,831
MEMS components	1,083	1,013	1,201	1,327	1,579
Other products	16	43	30	36	33
<b>Total</b>	<b>17,140</b>	<b>17,667</b>	<b>20,432</b>	<b>23,355</b>	<b>28,166</b>

Source: Company, DBS HK

## AAC Technologies Holdings

### Income Statement (RMB m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Revenue	17,140	17,667	20,432	23,355	28,166
Cost of Goods Sold	(12,913)	(13,302)	(16,017)	(18,404)	(22,399)
<b>Gross Profit</b>	<b>4,227</b>	<b>4,365</b>	<b>4,415</b>	<b>4,950</b>	<b>5,767</b>
Other Opng (Exp)/Inc	(2,878)	(2,882)	(2,963)	(3,386)	(4,082)
<b>Operating Profit</b>	<b>1,350</b>	<b>1,483</b>	<b>1,451</b>	<b>1,564</b>	<b>1,685</b>
Other Non Opg (Exp)/Inc	443	297	370	333	352
Associates & JV Inc	0	(1)	0	0	0
Net Interest (Exp)/Inc	(294)	(367)	(428)	(444)	(499)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	148	1	58	66	79
<b>Pre-tax Profit</b>	<b>1,648</b>	<b>1,413</b>	<b>1,451</b>	<b>1,519</b>	<b>1,617</b>
Tax	(147)	(120)	(158)	(166)	(176)
Minority Interest	6	23	7	9	(12)
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>1,507</b>	<b>1,316</b>	<b>1,300</b>	<b>1,362</b>	<b>1,428</b>
Net Profit before Except.	1,359	1,315	1,242	1,297	1,349
EBITDA	4,271	4,521	4,754	5,105	5,599
<b>Growth</b>					
Revenue Gth (%)	(4.2)	3.1	15.7	14.3	20.6
EBITDA Gth (%)	(12.2)	5.9	5.1	7.4	9.7
Opg Profit Gth (%)	(45.4)	9.8	(2.1)	7.8	7.7
Net Profit Gth (%)	(32.2)	(12.6)	(1.2)	4.8	4.9
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	24.7	24.7	21.6	21.2	20.5
Opg Profit Margin (%)	7.9	8.4	7.1	6.7	6.0
Net Profit Margin (%)	8.8	7.5	6.4	5.8	5.1
ROAE (%)	7.4	6.1	5.8	5.8	5.9
ROA (%)	4.1	3.3	3.0	3.0	2.9
ROCE (%)	4.0	4.0	3.6	3.7	3.8
Div Payout Ratio (%)	7.1	30.6	30.6	30.6	31.2
Net Interest Cover (x)	4.6	4.0	3.4	3.5	3.4

Source: Company, DBS HK

## AAC Technologies Holdings

### Balance Sheet (RMB m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Net Fixed Assets	20,500	22,032	23,999	26,382	29,604
Invts in Associates & JVs	0	4	4	4	4
Other LT Assets	1,561	2,031	2,206	2,557	2,772
Cash & ST Invts	7,632	6,054	5,412	3,348	926
Inventory	3,995	5,695	5,674	7,007	8,137
Debtors	5,182	6,188	6,467	7,367	8,848
Other Current Assets	40	18	20	22	25
<b>Total Assets</b>	<b>38,911</b>	<b>42,022</b>	<b>43,783</b>	<b>46,689</b>	<b>50,317</b>
ST Debt	3,349	2,902	1,993	2,471	2,890
Creditors	5,263	6,203	6,835	7,848	9,544
Other Current Liab	768	562	487	468	459
LT Debt	5,055	6,903	7,913	8,234	8,516
Other LT Liabilities	2,656	2,949	3,037	3,154	3,330
Shareholder's Equity	21,159	21,811	22,834	23,837	24,916
Minority Interests	662	691	684	675	663
<b>Total Cap. &amp; Liab.</b>	<b>38,911</b>	<b>42,022</b>	<b>43,783</b>	<b>46,689</b>	<b>50,317</b>
Non-Cash Wkg. Capital	3,186	5,136	4,839	6,080	7,007
Net Cash/(Debt)	(771)	(3,752)	(4,494)	(7,357)	(10,480)
Debtors Turn (avg days)	114.6	117.5	113.0	108.1	105.1
Creditors Turn (avg days)	189.3	198.2	181.8	176.3	168.5
Inventory Turn (avg days)	133.9	167.5	158.6	152.3	146.7
Asset Turnover (x)	0.5	0.4	0.5	0.5	0.6
Current Ratio (x)	1.8	1.9	1.9	1.6	1.4
Quick Ratio (x)	1.4	1.3	1.3	1.0	0.8
Net Debt/Equity (X)	0.0	0.2	0.2	0.3	0.4
Net Debt/Equity ex MI (X)	0.0	0.2	0.2	0.3	0.4
Capex to Debt (%)	58.6	44.3	49.8	52.5	59.7
Z-Score (X)	3.6	3.5	3.5	3.5	NA

Source: Company, DBS HK

### Cash Flow Statement (RMB m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Pre-Tax Profit	1,648	1,413	1,451	1,519	1,617
Dep. & Amort.	2,478	2,743	2,932	3,208	3,562
Tax Paid	(147)	(120)	(158)	(166)	(176)
Assoc. & JV Inc/(loss)	0	1	0	0	0
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	263	(1,949)	296	(1,241)	(927)
Other Operating CF	1,658	108	52	103	172
<b>Net Operating CF</b>	<b>5,900</b>	<b>2,195</b>	<b>4,574</b>	<b>3,423</b>	<b>4,248</b>
Capital Exp.(net)	(4,921)	(4,341)	(4,934)	(5,622)	(6,812)
Other Invts.(net)	(82)	(457)	248	(124)	62
Invts in Assoc. & JV	0	(5)	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	321	556	87	248	210
<b>Net Investing CF</b>	<b>(4,682)</b>	<b>(4,247)</b>	<b>(4,599)</b>	<b>(5,498)</b>	<b>(6,539)</b>
Div Paid	(107)	(403)	(398)	(417)	(445)
Chg in Gross Debt	(8)	1,402	100	800	700
Capital Issues	0	0	0	0	0
Other Financing CF	777	(438)	(376)	(437)	(465)
<b>Net Financing CF</b>	<b>663</b>	<b>561</b>	<b>(674)</b>	<b>(55)</b>	<b>(210)</b>
Currency Adjustments	148	1	58	66	79
Chg in Cash	2,028	(1,489)	(642)	(2,063)	(2,423)
Opg CFPS (RMB)	4.66	3.44	3.55	3.87	4.29
Free CFPS (RMB)	0.81	(1.78)	(0.30)	(1.82)	(2.13)

Source: Company, DBS HK

## AAC Technologies Holdings

### Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	15-Nov-21	HK\$33.75	HK\$39.80	Buy
2:	28-Mar-22	HK\$18.22	HK\$24.70	Buy

Source: DBS HK

Analyst: Jim Au

Tsz Wang Tam

## AAC Technologies Holdings

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**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

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**FULLY VALUED** (negative total return, i.e., > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

\*Share price appreciation + dividends

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