

# Nexteer Automotive Group

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DBS Group Research . Equity

13 Jul 2022

## BUY

Last Traded Price (12 Jul 2022): HK\$5.68 (HSI : 20,845)  
 Price Target 12-mth: HK\$7.30 (29% upside) (Prev HK\$8.00)

### Analyst

Rachel Miu +852 36684191 rachel\_miu@db.com

### What's New

- Anticipate better 2H22 performance on strong EV market and restocking in North America to boost production
- Weak 1H22 expected; supply chain disruptions and pandemic lockdowns affecting product margin recovery
- New product sales, EV opportunities and market recovery to support revenue expansion
- Maintain BUY; HK\$7.30 TP based on 14x FY22F PE

### Price Relative



### Forecasts and Valuation

FY Dec (US\$m)	2020A	2021A	2022F	2023F
Turnover	3,032	3,359	3,626	4,242
EBITDA	314	369	478	590
Pre-tax Profit	114	114	196	293
Net Profit	117	118	168	253
Net Pft (Pre Ex) (core profit)	117	118	168	253
Net Profit Gth (Pre-ex) (%)	(49.8)	1.4	41.9	50.5
EPS (US\$)	0.05	0.05	0.07	0.10
EPS (HK\$)	0.37	0.37	0.53	0.79
Core EPS (US\$)	0.05	0.05	0.07	0.10
Core EPS (HK\$)	0.37	0.37	0.53	0.79
EPS Gth (%)	(49.8)	1.4	41.9	50.5
Core EPS Gth (%)	(49.8)	1.4	41.9	50.5
Diluted EPS (HK\$)	0.37	0.37	0.53	0.79
DPS (HK\$)	0.07	0.07	0.11	0.16
BV Per Share (HK\$)	5.89	6.12	6.57	7.25
PE (X)	15.5	15.3	10.8	7.2
CorePE (X)	15.5	15.3	10.8	7.2
P/Cash Flow (X)	4.3	6.3	3.9	3.7
P/Free CF (X)	6.7	20.8	6.9	6.1
EV/EBITDA (X)	4.9	4.4	3.1	2.3
Net Div Yield (%)	1.3	1.3	1.9	2.8
P/Book Value (X)	1.0	0.9	0.9	0.8
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE(%)	6.3	6.2	8.3	11.5
Earnings Rev (%)			(27)	(17)
Consensus EPS (US\$)			0.06	0.09
Other Broker Recs:		B:15	S:2	H:3

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

## Improving 2H22 outlook

### Investment Thesis

1H22 was hit by lockdowns and supply chain disruptions; cut FY22/23F earnings by 27%/17%. Business slowed in 2Q22, due to geopolitical tensions, supply chain disruptions and lockdowns. Hence, EBITDA margins are estimated to contract to 10-11% in 1H22 from 1H21's 12.3%. We have cut FY22/23F earnings by 27%/17% to factor in the weak 1H22 performance.

**Anticipate a stronger 2H22.** The recovery is expected to be supported by strong global NEV market, restocking, and China's auto stimulus policy. Nexteer is in active negotiations with its customers on cost pass-through to protect its product margins. After the disruptions in 2Q, Nexteer expects to secure more new orders in 2H. It targets to achieve about US\$6bn worth of new orders in FY22

**Medium-term business outlook remains promising.** The first steer-by-wire contract of US\$2bn from a new European customer is scheduled for production in 2025. Also, growing contribution from the EV business is another strong earnings catalyst, given that 25% of its backlog orders of US\$26.8bn are for EV related steering products.

### Valuation:

Our new TP is HK\$7.30, pegged to 14x FY22F PE, equivalent to its historical average PE. The stock is currently trading at about 11x FY22F PE.

### Where we differ:

Our FY22/23F net earnings are slightly higher than consensus on easing of supply chain disruptions to support production recovery.

### Key Risks to Our View:

Rising raw material costs, disruption to the supply chain, and demand slowdown could impact earnings outlook.

### At A Glance

Issued Capital (m shrs)	2,510
Mkt Cap (HKm/US\$m)	14,257 / 1,816
Major Shareholders (%)	
Retrieving...	23.1
Sze (Man Bok)	20.6
Artisan Partners Limited Partnership	6.0
Free Float (%)	50.3
3m Avg. Daily Val. (US\$m)	7.57
GICS Industry: Consumer Discretionary / Automobiles & Components	



Watchlist the stock on Insights Direct to receive prompt updates



## Nexteer Automotive Group

### WHAT'S NEW

#### Expect a better 2H22 after a bumpy 1H

We hosted an Electric Vehicle Sector Conference Call with Nexteer's management and we have summarized the Q&A session. Raw material cost pressure and pass-through mechanism and impact on EBITDA were the major concerns of investors.

Q: Does the increase in inflation rate have any impact on the company's operations?

A: There is significant global impact. In Europe, inflation together with the Russia-Ukraine war and chip shortage have created a weak economic outlook for the region. As for the US, vehicle supply was largely affected by chip shortage and channel inventory remains low, which led to supply and demand imbalance.

The management expects a stronger auto market in 2H22, supported by healthy demand boosted by China's auto stimulus measures, and more stable supply chain and restocking. US customers are more optimistic on production orders. Based on market estimates, global automobile production could grow by 15-20% this year (with North America at about 20% growth in volume production). Expansion of Nexteer's customer base should support decent 2H22 growth.

Q: Is Nexteer able to pass through higher raw material cost?

A: In FY21, 65% of total costs was passed on to customers. The target for this year is >60%. Nexteer is in constant negotiations with its customers to pass through more of the increase in raw material electronic components and logistic costs. At times, Nexteer's customers have been willing to make a one-off compensation payment to cover the sharp rise in costs.

Q: What is Nexteer's plan for new launches in 2022? What took place in 2Q22?

A: Due to Covid lockdowns in some Chinese cities in 1H22, some new launches in China were delayed to 2H22. In 2H 2022, there will be new models and brand names for the program launch. For full year, at least 30 new programs will be launched globally.

Q: Are there any new investment plans for the China market, especially the NEV segment?

A: We have no plan to build new plants in the near-term. The focus now is to increase the utilization rate, expand

the current factory production capacity and improve production line efficiency by increasing the number of production shifts.

In China, Nexteer differentiates itself by being selective in choosing customers, which tends to be the new pure EV players. It plans to expand its electric power steering (EPS) product line as well as to secure more Chinese customers. More affordable or upgraded versions of EPS will be introduced, and customized solutions are also provided, depending on customer demand.

Q: Are there any updates on the business with Tesla?

A: Our business with the global pure EV maker is meaningful. The customer is satisfied with our products and services. This year, we have more opportunities to work with Tesla, on the column business.

Q: Is Nexteer taking on any new projects for advanced driver assistance systems (ADAS)?

A: In late 2021, we launched a new EPS. Our new stowable column will be ready in 2024 for commercialization and steer-by-wire orders should start contributing to revenue by 2025. Currently, Ford F150 and Geely Zeekr 001 have adopted some of our new steering products.

Q: What is the EBITDA and FCF guidance for 2022?

A: Due to the volatile oil and commodity prices in 1H22, product margins were being impacted. The management expect some easing in raw material cost pressure in 2H22 and that could potentially lift the EBITDA margins. As this year's revenue is expected to return to 2019's level, FCF is also expected to improve as the company is more careful with the working capital management.

Q: What is your new business target for 2022?

A: In 2021, Nexteer secured about US\$6bn worth of new contracts, although it was slightly below budget. This year, the company aims to achieve similar level as 2021. Besides, steer-by-wire contracts will add to the new business, and the potential value could be huge.

Q: What is the Capex guidance for 2022/23?

Nexteer's capex is largely on investment in tangible assets. Our capex is estimated to be US\$140-150m this year, which is slightly higher than FY21's to support its new program launches.

## Nexteer Automotive Group

Q: What is the company dividend policy?

A: Dividend payout ratio will be maintained at 20%

Q: What is Nexteer's guidance for the next 3-5 years?

A: From 2021-2025, the company targets to achieve 15% annual revenue growth, supported by new programs planned launches and new businesses opportunities, such as steer-by-wire. Although current share of the EV business to total revenue is not significant, but given that 25% of total order backlog is related to the EV business, EV contribution is expected to rise rapidly in the future.

Q: Can you comment on performance of overseas factories?

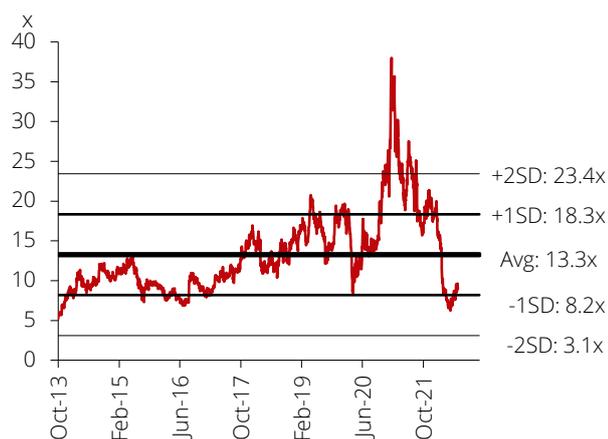
Currently, we have factories in Poland, Morocco, and Brazil. We are trying to improve EBITDA margin by switching supply chain from Europe and China to Morocco where the production cost is lower. We do expect to see rapid growth in the auto parts market, and we are confident in expanding our market share globally.

### Company Background

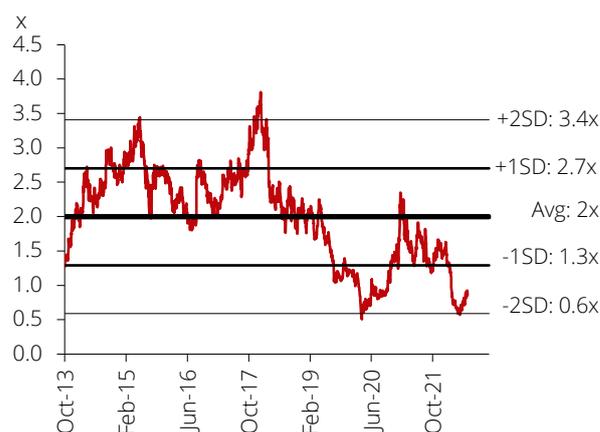
Nexteer is the world's leading producer of steering systems and counts major automakers as its customers. The company's key products are electric power steering (EPS) and hydraulic power steering (HPS) systems, and driveline. Its operations are spread across North America, Europe, South America, and Asia. Nexteer is collaborating with automakers and industry peers to develop power steering products for autonomous driving applications. The company is rapidly expanding its EV business exposure to ride on the global fast-growing trend.

### Historical PE and PB band

Forward PE band (x)



PB band (x)



Source: Thomson Reuters, DBS HK

## Nexteer Automotive Group

### Key Assumptions

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenue (US\$m) - North America	2,448.8	1,905.1	1,963.7	2,175.8	2,545.1
Europe and South America	484.3	485.6	585.5	544.0	636.3
Asia Pacific	642.6	641.4	809.5	906.6	1,060.5

Source: Company, DBS HK

### Segmental Breakdown (US\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
<b>Revenues (US\$ m)</b>					
EPS	2,409	2,058	2,326	2,385	2,797
HPS	138	120	137	130	145
Steering column (CIS)	496	344	318	479	537
Driveline	533	510	578	633	762
<b>Total</b>	<b>3,576</b>	<b>3,032</b>	<b>3,359</b>	<b>3,626</b>	<b>4,242</b>

Source: Company, DBS HK

### Income Statement (US\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenue	3,576	3,032	3,359	3,626	4,242
Cost of Goods Sold	(3,037)	(2,621)	(2,995)	(3,137)	(3,606)
<b>Gross Profit</b>	<b>539</b>	<b>411</b>	<b>363</b>	<b>490</b>	<b>636</b>
Other Opng (Exp)/Inc	(266)	(293)	(248)	(290)	(340)
<b>Operating Profit</b>	<b>273</b>	<b>119</b>	<b>115</b>	<b>200</b>	<b>297</b>
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	(4)	1	1	1	0
Net Interest (Exp)/Inc	(5)	(5)	(2)	(4)	(4)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>264</b>	<b>114</b>	<b>114</b>	<b>196</b>	<b>293</b>
Tax	(29)	8	12	(20)	(29)
Minority Interest	(2)	(6)	(8)	(9)	(11)
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>232</b>	<b>117</b>	<b>118</b>	<b>168</b>	<b>253</b>
Net Profit before Except.	232	117	118	168	253
EBITDA	495	314	369	478	590
<b>Growth</b>					
Revenue Gth (%)	(8.6)	(15.2)	10.8	8.0	17.0
EBITDA Gth (%)	(16.0)	(36.5)	17.3	29.7	23.4
Opg Profit Gth (%)	(35.7)	(56.5)	(3.0)	73.4	48.5
Net Profit Gth (%)	(38.8)	(49.8)	1.4	41.9	50.5
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	15.1	13.6	10.8	13.5	15.0
Opg Profit Margin (%)	7.6	3.9	3.4	5.5	7.0
Net Profit Margin (%)	6.5	3.9	3.5	4.6	6.0
ROAE (%)	13.3	6.3	6.2	8.3	11.5
ROA (%)	7.3	3.6	3.6	5.0	6.9
ROCE (%)	10.1	4.8	4.8	7.3	9.8
Div Payout Ratio (%)	35.1	20.2	20.1	20.2	20.2
Net Interest Cover (x)	55.2	23.5	62.1	51.3	67.2

Source: Company, DBS HK

## Nexteer Automotive Group

### Interim Income Statement (US\$ m)

FY Dec	2H2019	1H2020	2H2020	1H2021	2H2021
Revenue	1,743	1,211	1,821	1,734	1,624
Cost of Goods Sold	(1,494)	(1,089)	(1,532)	(1,508)	(1,487)
<b>Gross Profit</b>	<b>250</b>	<b>122</b>	<b>289</b>	<b>226</b>	<b>137</b>
Other Oper. (Exp)/Inc	(137)	(151)	(142)	(133)	(115)
<b>Operating Profit</b>	<b>113</b>	<b>(29)</b>	<b>148</b>	<b>94</b>	<b>21</b>
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	(2)	0	1	0	0
Net Interest (Exp)/Inc	(3)	(2)	(3)	(1)	(1)
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>109</b>	<b>(31)</b>	<b>146</b>	<b>93</b>	<b>21</b>
Tax	(7)	34	(26)	(6)	18
Minority Interest	(1)	(2)	(4)	(4)	(4)
<b>Net Profit</b>	<b>101</b>	<b>1</b>	<b>115</b>	<b>83</b>	<b>35</b>
Net profit bef Except.	101	1	115	83	35

### Growth

Revenue Gth (%)	(6.5)	(33.9)	4.5	43.3	(10.8)
Opg Profit Gth (%)	(38.6)	(118.1)	30.6	(424.5)	(85.4)
Net Profit Gth (%)	(43.7)	(99.0)	14.0	6,290.7	(69.4)

### Margins

Gross Margins (%)	14.3	10.1	15.9	13.1	8.4
Opg Profit Margins (%)	6.5	(2.4)	8.1	5.4	1.3
Net Profit Margins (%)	5.8	0.1	6.3	4.8	2.2

Source: Company, DBS HK

### Balance Sheet (US\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Net Fixed Assets	990	1,009	989	1,027	1,061
Invts in Associates & JVs	20	22	23	27	31
Other LT Assets	730	778	834	819	792
Cash & ST Invts	602	553	327	524	745
Inventory	266	234	289	312	337
Debtors	545	593	626	666	752
Other Current Assets	107	116	119	131	144
<b>Total Assets</b>	<b>3,259</b>	<b>3,306</b>	<b>3,206</b>	<b>3,506</b>	<b>3,862</b>
ST Debt	59	249	84	84	84
Creditors	592	657	667	700	735
Other Current Liab	214	202	191	233	253
LT Debt	249	0	0	70	140
Other LT Liabilities	294	277	262	263	264
Shareholder's Equity	1,812	1,882	1,955	2,099	2,318
Minority Interests	40	39	48	57	67
<b>Total Cap. &amp; Liab.</b>	<b>3,259</b>	<b>3,306</b>	<b>3,206</b>	<b>3,506</b>	<b>3,862</b>
Non-Cash Wkg. Capital	112	84	176	175	245
Net Cash/(Debt)	294	305	242	370	521
Debtors Turn (avg days)	54.8	68.5	66.2	65.0	61.0
Creditors Turn (avg days)	74.4	94.0	88.1	87.2	79.0
Inventory Turn (avg days)	32.5	37.6	34.8	38.3	35.7
Asset Turnover (x)	1.1	0.9	1.0	1.1	1.2
Current Ratio (x)	1.8	1.4	1.4	1.6	1.8
Quick Ratio (x)	1.3	1.0	1.0	1.2	1.4
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	64.8	60.2	237.0	129.5	89.1
Z-Score (X)	NA	NA	NA	NA	NA

Source: Company, DBS HK

## Nexteer Automotive Group

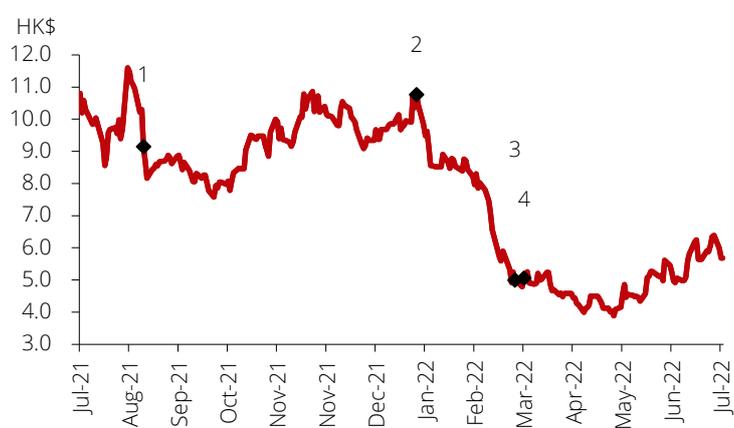
### Cash Flow Statement (US\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Pre-Tax Profit	264	114	114	196	293
Dep. & Amort.	226	195	253	278	293
Tax Paid	(18)	(29)	8	12	(20)
Assoc. & JV Inc/(loss)	0	0	0	0	0
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	(2)	87	(76)	(30)	(78)
Other Operating CF	21	52	(11)	6	8
<b>Net Operating CF</b>	<b>491</b>	<b>420</b>	<b>287</b>	<b>462</b>	<b>496</b>
Capital Exp.(net)	(199)	(150)	(200)	(200)	(200)
Other Invt. (net)	(6)	(2)	(5)	(4)	(3)
Invt. in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(168)	(136)	(81)	(100)	(100)
<b>Net Investing CF</b>	<b>(373)</b>	<b>(288)</b>	<b>(286)</b>	<b>(304)</b>	<b>(303)</b>
Div Paid	(78)	(90)	(24)	(24)	(34)
Chg in Gross Debt	(109)	(83)	(171)	63	61
Capital Issues	0	0	0	0	0
Other Financing CF	2	(14)	(21)	0	0
<b>Net Financing CF</b>	<b>(184)</b>	<b>(187)</b>	<b>(215)</b>	<b>40</b>	<b>27</b>
Currency Adjustments	(6)	7	(13)	0	0
Chg in Cash	(73)	(48)	(227)	198	221
Opg CFPS (US\$)	0.20	0.13	0.14	0.20	0.23
Free CFPS (US\$)	0.12	0.11	0.03	0.10	0.12

Source: Company, DBS HK

**Nexteer Automotive Group**

**Target Price & Ratings History**



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	18-Aug-21	HK\$9.14	HK\$14.00	Buy
2:	20-Jan-22	HK\$10.36	HK\$14.00	Buy
3:	17-Mar-22	HK\$5.24	HK\$8.00	Buy
4:	22-Mar-22	HK\$4.79	HK\$8.00	Buy

Source: DBS HK

Analyst: Rachel Miu

## Nexteer Automotive Group

DBS HK recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

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

**HOLD** (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

**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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Sources for all charts and tables are DBS HK unless otherwise specified.

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**DBS Bank (Hong Kong) Limited**

13<sup>th</sup> Floor One Island East, 18 Westlands Road, Quarry Bay, Hong Kong

Tel: (852) 3668-4181, Fax: (852) 2521-1812

## Nexteer Automotive Group

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### DBS Regional Research Offices

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#### HONG KONG

DBS Bank (Hong Kong) Ltd

Contact: Dennis Lam

13th Floor One Island East,

18 Westlands Road, Quarry Bay, Hong Kong

Tel: 852 3668 4181

Fax: 852 2521 1812

e-mail: dbsvhk@dbs.com

#### SINGAPORE

DBS Bank Ltd

Contact: Paul Yong

12 Marina Boulevard,

Marina Bay Financial Centre Tower 3

Singapore 018982

Tel: 65 6878 8888

e-mail: groupresearch@dbs.com

Company Regn. No. 196800306E

#### INDONESIA

PT DBS Vickers Sekuritas (Indonesia)

Contact: Maynard Priajaya Arif

DBS Bank Tower

Ciputra World 1, 32/F

Jl. Prof. Dr. Satrio Kav. 3-5

Jakarta 12940, Indonesia

Tel: 62 21 3003 4900

Fax: 6221 3003 4943

e-mail: indonesiaresearch@dbs.com

#### THAILAND

DBS Vickers Securities (Thailand) Co Ltd

Contact: Chanpen Sirithanarattanakul

989 Siam Piwat Tower Building,

9th, 14th-15th Floor

Rama 1 Road, Pathumwan,

Bangkok Thailand 10330

Tel. 66 2 857 7831

Fax: 66 2 658 1269

e-mail: research@th.dbs.com

Company Regn. No 0105539127012

Securities and Exchange Commission, Thailand