

# China / Hong Kong Industry Focus

## China Hardware Sector

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DBS Group Research . Equity

14 Nov 2023

### Don't overlook iPhone suppliers

- **Recent outperformance of Android suppliers should have largely priced in Huawei's boost; expect iPhone suppliers to catch up, driven by solid shipment growth**
- **iPhone 15 shipment likely exceeds previous market expectations by 10%, based on promising presales data**
- **Huawei's gain should be at the expense of other Android makers, except for Xiaomi which flagship sales have been robust**
- **Raised earnings and maintain BUY on [Luxshare \(002475CH\)](#)/ [Xiaomi \(1810 HK\)](#), with our FY24F forecast 12%/ 18% above consensus**

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#### Recommendation & valuation

Company Name	Currency	Price	Target Price	Recom	Mkt Cap
		Local\$	Local\$		US\$m
<a href="#">Xiaomi (1810 HK)</a>	HKD	15.86	18.90	BUY	50,879
<a href="#">Luxshare (002475 CH)</a>	RMB	31.89	55.00	BUY	31,286

Source: Thomson Reuters, DBS Bank (Hong Kong) Limited ("DBS HK")

#### Growing optimism for Huawei but impact on suppliers limited.

"Mate 60 Pro" has received an overwhelming reception in China. Huawei increased its 2023 shipment targets by 33%, aiming for 40m units. We expect it to further grow by 94% in 2024. However, this growth is likely to come at the expense of other Android brands. Android suppliers will face a mixed impact as they serve multiple Android brands. In contrast, iPhone 15 has shown promising presales data, reflecting a more positive outlook despite the initial scepticism. We believe FY23 iPhone 15 shipment could reach 81-83m unit, c.10% higher than previous market expectations of 73-75m units, with growth to stay solid at 5% in 2024, outpacing global shipment growth.

**Huawei's incremental shipment is already priced in.** We expect recent share price gains of Android suppliers, ranging from c.7% to 55% since Sept, should have factored in Huawei's boost as Huawei only accounts for 1.5% of the total Android shipment. Meanwhile, most iPhone suppliers like Luxshare have underperformed compared to Android players, with room to catch up on stronger shipments – we lifted FY23F/24F earnings forecast for Luxshare by 1.6%/5.9%. For 2024, we remain positive on overall smartphone shipment outlook with a projected 4.5% y-o-y recovery (Android: 4.4%; iPhone 5%), fuelled by a peak of handset replacement cycles. This, coupled with relatively attractive valuations of c.-1SD below the historical PE mean, should pave way for further re-rating in 2024.

#### Raised FY24F earnings forecast for both Luxshare and Xiaomi.

Apart from Huawei, Xiaomi will surpass competitors and reinforce its market position in 4Q23, thanks to its significantly upgraded flagship with an unbeatable price and the growth momentum from an early launch. We raised Xiaomi's earnings forecast by 3.9%/5.9% in FY23F/24F, with FY24F earnings 18% above consensus. Suppliers like Luxshare, with strong ties to Apple, are also poised to benefit from relatively strong iPhone shipments in 2023/ 2024. Our FY24F forecast is 12% above consensus.

## China Hardware Sector

### Introduction

Huawei has returned to the premium smartphone market with the launch of the Mate 60 Pro. The product received an overwhelming reception in China, with the support of the technological breakthrough in its system-on-chip (SoC). At the same time, the iPhone 15 has shown promising presales data. Xiaomi also launched its Xiaomi 14 model earlier than expected, with its specifications expected to be comparable to that of the iPhone 15 Pro.

This development has drawn investor interest back to the China hardware sector and component suppliers along the smartphone value chain, which have been suffering due to sluggish global smartphone shipments. Android suppliers' share prices have risen from c.7% to c.55% since Sept. In this report, we will reassess the cumulative impact of these developments on the stocks we cover.

### Huawei's comeback with Mate 60 Pro

Huawei's newest flagship, the "Mate 60 Pro", stands as a testament to China's ability to overcome the US tech ban. The initial reception in China has been overwhelming, with record-breaking sales, as evidenced by the extensive queues witnessed at retail stores across multiple cities.

The Chinese media regards the Mate 60 Pro a technological breakthrough due to its "7nm" 5G-enabled System-on-Chip (SoC), the Kirin 9000s. According to our channel check, this SoC is fabricated by SMIC using the "N+2" lithography technology. This method aims to enhance the transistor density on the chips by providing additional exposure with a DUV lithography machine.

Chips produced with this technology are predicted to have a lower yield and a higher manufacturing cost. Nevertheless, they provide the new phone with 7nm-like performance and 5G capabilities. Meanwhile, the flagship smartphones from competitors are equipped with 4nm chips, like Qualcomm's Snapdragon 8 Gen 2 SoC, and are priced similarly. We expect Huawei's SoC technology will stay with 7nm, as their chip development focus will remain on N+2 technology in the coming two years, with a goal of improving its yield.

The remarkable sales of Huawei's new release, backed by its strong brand loyalty, have set a promising precedent. This upward trend is expected to continue with subsequent products. Huawei escalated its shipment targets by 33%, aiming for a robust 40m units in 2023, suggesting a y-o-y growth of 126%, according to STCN's report. We expect the shipment to further grow 94% y-o-y to c.77.5m units in 2024.

Following our channel checks, we anticipate that Huawei's increased shipments will likely cannibalise the market share of incumbent players such as Honor, Oppo, and Vivo. This scenario implies a shift in market dynamics rather than a substantial surge in overall smartphone shipments.

### Mild boost to the overall Android shipment growth

We project Huawei's market share in smartphones to rebound from 1.5% in 2022 to 3.5% in 2023 and 6.4% in 2024, while that of other Android brands (except Xiaomi) would decrease from 67.1% in 2022 to 63.7% in 2023 and 60.0% in 2024. The overall Android phone shipment is expected to rebound by 4.4% y-o-y in 2024, mainly driven by replacements.

### iPhone 15 presales exceeding original expectations

Apple's iPhone shipments have consistently been a focal point of market analysis. The current debate revolves around whether the iPhone 15 can maintain its trajectory of market-beating growth in the global smartphone arena. The market sentiment initially appeared pessimistic regarding iPhone 15 shipments for 2023.

Some broker research revised the 2023 iPhone 15 series shipment forecast in August 2023, decreasing it from c.85m units to a range of 73-77m units in early September. This adjustment signifies a transition from 9% y-o-y growth to a 3.8% y-o-y decline at the midpoint. This shift is attributed to the sustained weak consumer sentiment and manufacturing capacity bottlenecks. However, the presales data paints a different picture and led to a revision in the forecast.

The iPhone 15's presales outperformed that of its predecessor the iPhone 14 on the first-day post-launch on JD.com, with the numbers continuing on an upward curve. Furthermore, the preorders for the iPhone 15 and iPhone 15 Plus in India surged by approximately 50% in comparison to the iPhone 14 series in 2022, as per a report from Indo-Asian News Service. While some industry research like TrendForce has already slightly increased iPhone 15 shipment predictions for 2023, from an expected range of 73-77m units to 80-85m units. We believe the FY23 iPhone 15 shipment could reach 81-85m units, c.10% higher than previous market expectations of 73-77m units.

### iPhone shipments continue to grow by 5% in 2024

Therefore, we anticipate iPhone shipment to grow by 5% y-o-y in 2024, continues to outpace global smartphone shipment growth and sustain its market share gains. The growth momentum is driven by strong product innovation, like the powerful A17 pro SoC, and user loyalty.

Overall, the market is only anticipating a mild recovery of 2.3% y-o-y in global smartphone shipments in 2H23 due to

**China Hardware Sector**

the prolonged uncertainty in the global economy. However, we expect consumer sentiment to gradually improve on the back of these buzz-generating flagships, which have successfully drawn customers' attention back to the smartphone market. We anticipate the recovery to accelerate to a growth of 4.5% y-o-y in 2024, driven by handset replacements occurring three years after the last peak in premium phone replacements. We expect Android and iPhone shipments to increase by 4.4% y-o-y and 5% y-o-y in 2024 respectively.

All in all, these two developments are set to influence the smartphone supply chain players covered in our stock report as follows:

**Impact on smartphone supply chain**

Suppliers	Apple product's exposure	Huawei supplier?	Impact of Huawei's incremental shipments	Impact of strong iPhone 15 presales
Sunny Optical	2.80%	Yes	Android smartphones contribute the majority of its revenue and profit <ul style="list-style-type: none"> <li>Mixed impact, as it benefitted from incremental shipments but suffered from other brands' shipment losses</li> </ul>	<ul style="list-style-type: none"> <li>Minimal impact, small revenue contribution from iPhone</li> </ul>
Q Tech	0%	Yes	<ul style="list-style-type: none"> <li>Mildly negative impact from the potential drop in shipments of Oppo and Vivo</li> </ul>	<ul style="list-style-type: none"> <li>No impact, as no iPhone exposure</li> </ul>
BYD Electronics	70% (of consumer electronics), minimal exposure to iPhone	Yes	<ul style="list-style-type: none"> <li>Mixed impact, as it provides components for all Android phones</li> </ul>	<ul style="list-style-type: none"> <li>Initially penetrated iPhone value chain in 2022</li> <li><b>Small contribution from iPhone</b></li> <li>Minimal impact on the strong iPhone 15 sales</li> </ul>
Luxshare	73.3%	Yes	<ul style="list-style-type: none"> <li>Mixed impact, as it benefitted from incremental shipments</li> <li>But it suffered from other brands' shipment losses</li> </ul>	<ul style="list-style-type: none"> <li>Potential beneficiary of the strong iPhone 15 sales</li> <li><b>Assembles c.10% of iPhone 15 shipments</b>, including premium model</li> </ul>

Source: DBS HK

**Xiaomi's early launch of flagship**

Despite the threat from Huawei, Xiaomi is poised to maintain its market position through product innovation and a savvy sales strategy.

Xiaomi just unveiled a new flagship smartphone, Xiaomi 14, incorporating significant upgrades with next-generation SoC from Qualcomm, premium Leica cameras, and a self-developed operating system. The starting price for this flagship series is Rmb3,999 vs. Huawei Mate 60 Pro's Rmb6,999 and the iPhone 15 Pro's Rmb7,999, which makes it highly competitive against other Android phones at this price range.

The Xiaomi 14 series is also the first to feature the Snapdragon 8 Gen 3 SoC. Besides the fact that Qualcomm and Xiaomi each hold a c.5% ownership in the other, the bond between Xiaomi and its primary chip suppliers has

been strengthening since the former head of Qualcomm's Chinese operations joined Xiaomi in 2015. Their joint work on the application of Meter-Level Positioning for Mobile recently underscored this partnership.

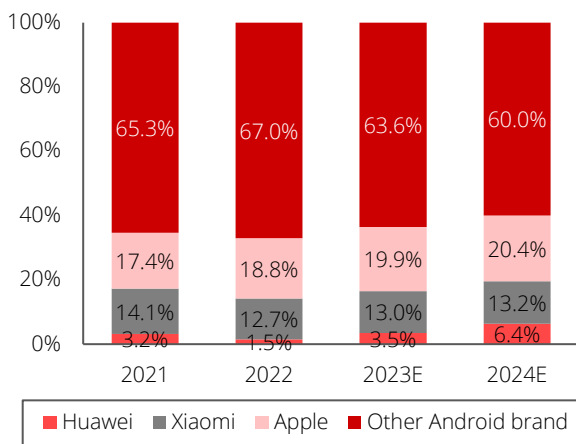
This solid strategic relationship has enabled the Xiaomi 14 series to be the first line-up to be powered by the Snapdragon 8 Gen 3 SoC. The new SoC is 30% faster and 20% more efficient than its predecessor, Gen 2, and can provide an enhanced performance of the cameras, AI capabilities, connectivity, etc. in the phone.

With early access to the latest SoC, Xiaomi managed to debut its flagship on 26 October, ahead of the late December release of its previous model last year. This strategic release positions the latest flagship smartphone to benefit from the year-end peak sales season, which includes the "Double 11" festival. Given this, we project the sales

from this early flagship launch to boost Xiaomi's GMV, potentially exceeding last year's Rmb17bn.

Even amid stiff competition with Huawei and Apple, Xiaomi held steady, preserving 14% of the global smartphone market share. Given the momentum of the early launch of its flagship model, we anticipate Xiaomi would witness 30% y-o-y growth in its smartphone shipments in 4Q23. This positive trend is expected to persist going into 2024 with projected 7.5% y-o-y growth.

**Market share forecast for Huawei, Xiaomi and Apple**



Source: IDC, DBS HK

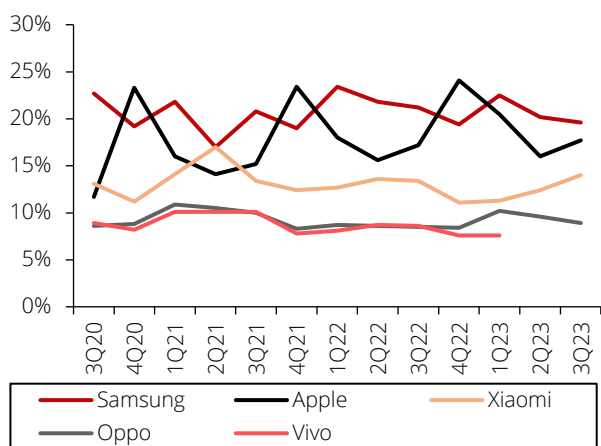
China Hardware Sector

Latest flagship comparison (Apple vs. Huawei vs. Xiaomi)

Brand	Apple	Huawei	Xiaomi
Model	iPhone 15 Pro (512 GB)	Mate 60 Pro (12GB RAM, 512GB)	Xiaomi 14 (16GB RAM, 512GB)
Price	Rmb10,999	Rmb6,999	Rmb4,599
SoC	A17 Pro (3nm)	Kirin 9000S (7nm)	Snapdragon 8 Gen 3 (4nm)
Cameras	Main: 48MP f/1.78 Wide: 12MP, f/1.78 Telephoto: 12MP 2x; 12MP 3x	Main: 50MP f/1.4-f/4.0 Wide: 12MP, f/2.2 Telephoto: 48MP, 3.5x, f/3.5	<b>All Leica premium lenses:</b> Main: 50MP f/1.6 Wide: 50MP, f/2.2 Telephoto: 50MP, 3.2x, f/2.0
SoC Multi-core performance score (Geekbench 6)	7261	3571	7494
GPU's performance (3DMark WildLife Extreme)	4075 score / 24.4 FPS	1537 score	5338 score / 32 FPS
Screen	OLED, 460 ppi density	OLED, 423 ppi density	OLED, c.460 ppi density

Source: DBS HK

Global smartphone market share



Source: IDC, DBS HK

Conclusion:

Huawei will gain back market share, mostly at the expense of other Android brands. We expect stocks focusing on Android phone businesses, like Q Tech, to face a minimal impact to fundamentals. Their share prices have risen from 7% to 55% since Sept, outperforming that of Apple-focused suppliers like Luxshare and BYDE. We believe the recent share price movement of the Android component suppliers has largely factored in positives from the latest launch of the flagship smartphones, which would be partially offset by weaker shipment in other Android phones.

However, we remain positive on the smartphone supply chain sector in 2024, as we estimate the smartphone

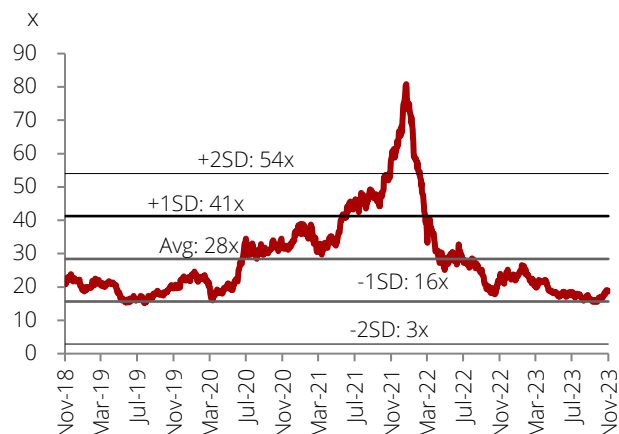
shipments have already bottomed out and will continue to recover. Valuations remain at relatively low levels, c.-1SD below historical PE mean, following a deep correction since the beginning of 2023. We expect the sector to be re-rated upon the solid growth in smartphone shipments expected in 2024.

Meanwhile, we like stocks with significant or increasing Apple exposure such as Luxshare. This company will benefit from the iPhone's better-than-expected shipments. We forecast that incremental iPhone shipment orders will boost Luxshare's projected FY23/24F net profit by 1.6%/5.9%, respectively. Our FY24F earnings forecast is 11.9% higher than the market consensus. As a result, we revised Luxshare's TP upwards to Rmb55.0 (from Rmb52.0 previously), based on 27.0x FY24F PE, pegged to its historical PE average. We retain BUY considering its promising market share gains within Apple's value chain and revenue growth from AI servers and the automotive sector.

Regarding smartphone vendors, we believe Xiaomi would maintain its share and showcase its resilience in the anticipated recovery of the smartphone sector in 4Q23 and throughout 2024. We have increased our earnings forecast by 3.9% for FY23 and by 5.9% for FY24, driven by stronger-than-anticipated smartphone shipment sales. Our FY24F earnings forecast is 17.9% higher than the market consensus. We lifted Xiaomi's TP to HK\$18.9 (from HK\$18.0 previously), based on 27x FY24F PE, below the average historical forward PE of 32x since its IPO. We maintain BUY as we project a 16% rebound in Xiaomi's FY24F smartphone revenue, driven by (1) the gross margin enhancement resulting from smartphone premiumisation and (2) shipment recovery.

China Hardware Sector

Sector PE (MC wt. avg) - 5 Year



Source: Thomson Reuters, DBS HK

Peers table

Company Name	Currency	Code	Target		Recom	Fiscal Yr	PE		Yield		P/Bk		EV/EBITDA		ROE		P/S	
			Price	Price			23F	24F	23F	24F	23F	24F	23F	24F	23F	24F	23F	24F
Hua Hong Semiconductor*	HKD	1347 HK	18.56	22.00	HOLD	Dec	15.2	15.7	0.0	0.0	0.7	0.7	3.4	4.1	6.2	4.5	1.4	1.3
Semicon.Mnfg.Intl.*	HKD	981 HK	22.05	23.30	BUY	Dec	21.3	18.9	0.0	0.0	1.1	1.0	7.8	7.2	5.3	5.7	2.7	2.0
Asmpt*	HKD	522 HK	70.35	71.00	HOLD	Dec	24.0	14.7	3.6	2.5	1.8	1.7	10.7	7.3	7.6	11.8	1.8	1.6
Byd Electronic (Intl.)*	HKD	285 HK	37.05	48.00	BUY	Dec	19.5	14.0	1.0	1.4	2.7	2.3	10.4	8.1	14.7	17.9	0.6	0.5
Luxshare Precn.Ind.'A'*	CNY	002475 CH	31.89	55.00	BUY	Dec	21.1	15.6	0.5	0.6	4.2	3.4	10.0	7.8	22.4	24.1	1.1	1.0
Sunny Optical Tech.(Gp.)*	HKD	2382 HK	71.2	79.00	BUY	Dec	48.0	20.1	0.7	0.4	3.2	2.8	14.4	8.6	6.8	14.7	2.4	1.9
Q Technology (Group)*	HKD	1478 HK	4.55	4.12	BUY	Dec	32.8	11.9	0.0	0.5	1.0	0.9	9.7	5.9	3.2	8.4	0.4	0.3
Xiaomi*	HKD	1810 HK	15.86	18.90	BUY	Dec	29.1	24.2	0.0	0.0	2.3	2.1	21.7	15.5	8.4	9.1	1.3	1.2
Lenovo Group*#	HKD	992 HK	9.43	7.40	HOLD	Mar	11.9	8.1	3.3	4.8	2.4	2.1	4.2	3.4	22.8	30.0	0.2	0.2

# FY24: FY25; FY25: FY26

Source: Thomson Reuters, \*DBS HK

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\*Share price appreciation + dividends

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