

## COMPANY UPDATE

### Xiaomi Corp (1810 HK)

3Q22 Results Preview: Still Deteriorating yoy But Stabilising Sequentially

**Xiaomi will report its 3Q22 earnings on 23 Nov 22. We expect the company's revenue to grow 10% yoy but remain flat qoq, and adjusted net profit to decline both 62% yoy and 6% qoq. While the sharp yoy decline is well-expected, the sequential decline should have stabilised, while inventory level has been improving since end-2Q22. Maintain BUY but trim target price to HK\$11.30.**

#### WHAT'S NEW

- **3Q22: Earnings decline should have stabilised.** We expect 3Q22 revenue to decline 9.9% yoy and remain largely flat qoq at Rmb70.3b, blended gross margins to fall 1.3ppt yoy but recover 0.2ppt qoq, and adjusted net profit to decline 62.2% yoy and 5.9% qoq to Rmb1,958m.

#### 3Q22 RESULTS ESTIMATES

Year to 31 Dec	3Q21	2Q22	3Q22F	yoy%	qoq %
Revenue	78,063	70,171	70,226	(10.0)	0.1
Smartphones	47,825	42,268	42,930	(10.2)	1.6
IoT & Lifestyle products	20,936	19,812	19,261	(8.0)	(2.8)
Internet services	7,338	6,971	7,035	(4.1)	0.9
Other	1,965	1,120	1,000	(49.1)	(10.7)
Gross Profit	14,292	11,768	11,950	(16.4)	1.5
Adjusted Net Profit	5,176	2,081	1,958	(62.2)	(5.9)
GPM (%)	18.3	16.8	17.0	(1.3)	0.2
Smartphones	12.8	8.7	9.1	(3.7)	0.4
IoT & Lifestyle products	11.6	14.3	14.5	2.9	0.2
Internet services	73.6	73.0	72.5	(1.1)	(0.5)

Source: Xiaomi, UOB Kay Hian

- **Smartphone shipment remained sluggish as expected.** As reported by IDC, Xiaomi Corp's (Xiaomi) smartphone shipment in 3Q22 declined 8.6% yoy but grew 2.5% qoq to 40.5m units, which is below our estimate of 43m units, although not entirely unexpected given the ongoing destocking across the smartphone value chain and poor end-demand in China and Europe, the two largest markets for Xiaomi. We expect ASP to marginally decline by 2% on higher mix from low-end smartphone sales in India and LATAM, while its margins should recover slightly on less promotion events. As such, we estimate the segment's revenue to decline 10.2% yoy but remain stable qoq at 1.6% growth to Rmb43b, while margins should decline 3.7ppt yoy but recover 0.4ppt qoq to 9.1%.

- **We see a parallel in the IoT & lifestyle segment.** We are expecting an 8% yoy decline in the segment's revenue to Rmb19b in 3Q22, on the back of sluggish demand for wearables and home appliances in domestic and foreign markets, as well as the ASP declines in key IoT products such as TVs. On the bright side, we are expecting gross margins to remain stable at 14.5% (vs 14.3% in 2Q22), thanks to moderating component costs and less promotional events.

#### KEY FINANCIALS

Year to 31 Dec (Rmbm)	2020	2021	2022F	2023F	2024F
Net turnover	245,866	328,309	289,835	310,824	361,171
EBITDA	11,561	23,263	14,181	19,137	23,173
Operating profit	9,853	20,201	11,222	15,943	20,837
Net profit (rep./act.)	20,356	19,339	4,079	11,557	15,906
Net profit (adj.)	13,006	22,040	8,820	11,557	15,906
EPS (Fen)	54.2	88.4	35.4	46.4	63.8
PE (x)	15.6	9.6	25.0	18.3	13.3
P/B (x)	1.9	2.5	1.7	1.5	1.5
EV/EBITDA (x)	11.7	5.8	9.5	7.1	5.8
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Net margin (%)	8.3	5.9	1.4	3.7	4.4
Net debt/(cash) to equity (%)	(44.3)	(20.6)	(19.0)	(21.8)	(25.7)
Interest cover (x)	4.1	12.5	5.8	7.7	12.1
ROE (%)	12.7	16.9	6.3	7.9	9.9
Consensus net profit	-	-	13,241	17,852	21,189
UOBKH/Consensus (x)	-	-	0.67	0.65	0.75

Source: Xiaomi, Bloomberg, UOB Kay Hian

## BUY

(Maintained)

Share Price	HK\$10.16
Target Price	HK\$11.30
Upside	+11.2%
(Previous TP)	HK\$12.30)

#### COMPANY DESCRIPTION

Xiaomi Corporation manufactures communication equipment and parts. The company produces and sells mobile phones, smart phone software, set-top boxes and related accessories. Xiaomi markets its products worldwide.

#### STOCK DATA

GICS sector	Communications Equipment
Bloomberg ticker:	1810 HK
Shares issued (m):	20,296
Market cap (HK\$m):	206,207
Market cap (US\$m):	30,325
3-mth avg daily t'over (US\$m):	157.8

#### Price Performance (%)

52-week high/low HK\$22.00/HK\$8.30

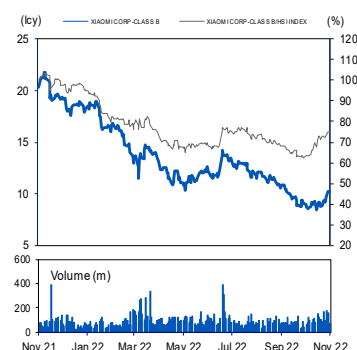
1mth	3mth	6mth	1yr	YTD
11.9	(13.8)	(8.5)	(50.1)	(46.2)

#### Major Shareholders

	%
Lei Jun	9.31%
Lin Bin	9.22%

FY22 NAV/Share (RMB)	6.69
FY22 Net Debt/Share (RMB)	1.27

#### PRICE CHART



Source: Bloomberg

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- **Internet services business to face pressure from low advertising spending in China.** We are expecting the segment's China business to register a 10.7% yoy and 0.9% qoq decline to Rmb5.3b, primarily due to the deteriorating advertising spending by domestic corporates amid the ongoing COVID-19 situation. This will be partially offset by a resilient 18.5% yoy and 6.7% qoq growth in the overseas business on the back of MAU expansion (+8% qoq to 440m). Overall, we expect the internet service segment's revenue to decline 4.1% yoy to Rmb7.0b, and its margins to decline slightly by 0.5ppt to 72.5% due to deterioration in the high-margin advertising business.

### STOCK IMPACT

- **Despite sluggish sales growth, market dynamics for Android smartphone supply chain should become more favourable through 4Q22-1Q23**, as according to our understanding, the destocking through the Android value chain (including Xiaomi) has been going smoothly in 3Q22, and the inventory levels for the Chinese brands are now at a healthier level. With the positive reception in the 11.11 sales so far (on the back of pent-up demand and sharper discounts on older models), we are now in line with the market's view that the destocking period can end by 1Q23. As such, we now believe 4Q22 will be the trough level for the Android value chain in the current downcycle.
- **However, we see no significant recovery in end-demand in 1H23**, given the ongoing global recession. As such, we trim our shipment forecast for Xiaomi by 3.1%/4.7%/3.2% to 162m/174m/199m units for 2022-24F respectively. We trim down our gross margin assumptions for smartphones by 0.7ppt/0.5ppt to 9.3%/9.5% in 2022-23 as we expect Xiaomi to provide more discounts/less aggressive pricing during the economic downturn. We also trimmed down internet services margins by 0.7ppt to 72.3% in 2022F, given the lower mix in advertising revenue.

### EARNING REVISION/RISK

- **We trimmed our 2022-24 adjust earnings estimates by 4.1%/9.7%/10.7% to Rmb8,820m/Rmb11,557m/Rmb15,906m respectively** as we cut our shipment and margins assumption for 2022-24 to reflect our cautious view on the end-demand of smartphones in the coming three years amid a softer economic outlook.
- **Risks:** a) Worse-than-expected share loss in the domestic market, b) intensifying competition in Europe and Latin America, c) sustained lockdowns in China, and d) further geopolitical risks in India.

### VALUATION/RECOMMENDATION

- **Maintain BUY, and cut target price to HK\$11.30**, as we factor in lower earnings estimates. Our target price is now based on 21.0x 2023F PE, still pegged to 0.5SD below mean. We believe the market is aware of the risks on Xiaomi, and expectations have already reached the lowest point with a visible trough in 4Q22-1Q23. As such, we are now turning more positive on the company.

### CHANGES TO KEY ASSUMPTIONS

(Rmbm)	OLD			New			Change (%)		
	2022F	2023F	2024F	2022F	2023F	2024F	2022F	2023F	2024F
Revenue	305,290	336,011	390,898	289,835	310,824	361,171	(5.1)	(7.5)	(7.6)
Smartphone	185,075	212,691	250,910	176,762	194,024	232,413	(4.5)	(8.8)	(7.4)
IoT and Lifestyle products	84,980	84,980	97,727	80,731	80,731	88,804	(5.0)	(5.0)	(9.1)
Internet services	28,987	32,092	36,012	28,342	32,069	35,953	(2.2)	(0.1)	(0.2)
Smartphone shipment (m units)	167	183	205	162	174	199	(3.1)	(4.7)	(3.2)
Smartphone ASP (Rmb)	1,109	1,164	1,222	1,092	1,114	1,170	(1.5)	(4.3)	(4.3)
Gross Profit	52,677	58,556	67,215	49,480	54,796	63,692	(6.1)	(6.4)	(5.2)
Reported NP	9,197	12,802	17,814	8,820	11,557	15,906	(4.1)	(9.7)	(10.7)
GPM (%)	17.3	17.4	17.2	17.1	17.6	17.6	(0.2)	0.2	0.4
Smartphones	10.0	10.0	10.0	9.3	9.5	10.0	(0.7)	(0.5)	-
IoT and Lifestyle products	14.5	15.5	15.5	15.0	15.5	15.5	0.5	-	-
Internet Services	73.0	73.0	73.0	72.3	73.0	73.0	(0.7)	-	-

Source: Xiaomi, UOB Kay Hian

### PROFIT & LOSS

Year to 31 Dec (Rmbm)	2021	2022F	2023F	2024F
Net turnover	328,309	289,835	310,824	361,171
EBITDA	23,263	14,181	19,137	23,173
Deprec. & amort.	(3,062)	(2,959)	(3,194)	(2,336)
EBIT	20,201	11,222	15,943	20,837
Total other non-operating income	5,828	(4,201)	-	-
Associate contributions	275	(139)	-	-
Net interest income/(expense)	(1,612)	(1,937)	(2,060)	(1,728)
<b>Pre-tax profit</b>	<b>24,417</b>	<b>5,083</b>	<b>13,883</b>	<b>19,109</b>
Tax	(5,134)	(1,017)	(2,360)	(3,248)
Minorities	56	12	34	46
<b>Net profit</b>	<b>19,339</b>	<b>4,079</b>	<b>11,557</b>	<b>15,906</b>
Net profit (adj.)	22,040	8,820	11,557	15,906

### BALANCE SHEET

Year to 31 Dec (Rmbm)	2021	2022F	2023F	2024F
Fixed assets	6,965	13,030	18,900	25,697
Other LT assets	100,076	99,051	97,988	96,855
Cash/ST investment	23,512	29,531	36,072	46,100
Other current assets	162,340	133,759	173,472	161,813
<b>Total assets</b>	<b>292,892</b>	<b>275,371</b>	<b>326,431</b>	<b>330,464</b>
ST debt	5,527	12,998	12,998	12,998
Other current liabilities	110,200	81,141	120,678	108,851
LT debt	20,720	20,720	20,720	20,720
Other LT liabilities	19,012	19,012	19,012	19,012
Shareholders' equity	137,213	141,291	152,848	168,755
Minority interest	220	208	174	128
<b>Total liabilities &amp; equity</b>	<b>292,892</b>	<b>275,371</b>	<b>326,431</b>	<b>330,464</b>

### CASH FLOW

Year to 31 Dec (Rmbm)	2021	2022F	2023F	2024F
<b>Operating</b>	<b>9,785</b>	<b>8,485</b>	<b>16,600</b>	<b>19,757</b>
Pre-tax profit	24,417	5,083	13,883	19,109
Tax	(2,442)	(1,017)	(2,360)	(3,248)
Deprec. & amort.	3,062	2,959	3,194	2,336
Associates	(275)	139	-	-
Working capital changes	(9,363)	(478)	(176)	(168)
Non-cash items	(5,613)	1,799	2,060	1,728
Other operating cashflows	-	-	-	-
<b>Investing</b>	<b>(45,008)</b>	<b>(8,000)</b>	<b>(8,000)</b>	<b>(8,000)</b>
Capex (growth)	(7,169)	(8,000)	(8,000)	(8,000)
Investments	(209,603)	-	-	-
Proceeds from sale of assets	170,237	-	-	-
Others	1,527	-	-	-
<b>Financing</b>	<b>4,499</b>	<b>5,534</b>	<b>(2,060)</b>	<b>(1,728)</b>
Dividend payments	-	-	-	-
Issue of shares	83	-	-	-
Proceeds from borrowings	22,529	30,000	30,000	30,000
Loan repayment	(13,301)	(22,529)	(30,000)	(30,000)
Others/interest paid	(4,812)	(1,937)	(2,060)	(1,728)
<b>Net cash inflow (outflow)</b>	<b>(30,724)</b>	<b>6,019</b>	<b>6,540</b>	<b>10,028</b>
Beginning cash & cash equivalent	54,752	23,512	29,531	36,072
Changes due to forex impact	(517)	-	-	-
<b>Ending cash &amp; cash equivalent</b>	<b>23,512</b>	<b>29,531</b>	<b>36,072</b>	<b>46,100</b>

### KEY METRICS

Year to 31 Dec (%)	2021	2022F	2023F	2024F
<b>Profitability</b>				
Gross margin	17.7	17.1	17.6	17.6
Pre-tax margin	8.2	2.1	4.5	5.3
Net margin	5.9	1.4	3.7	4.4
ROA	8.1	3.1	3.8	4.8
ROE	16.9	6.3	7.9	9.9
<b>Growth</b>				
Turnover	33.5	(11.7)	7.2	16.2
EBITDA	58.5	(15.1)	10.7	16.2
Pre-tax profit	12.9	(79.2)	173.1	37.6
Net profit	(5.0)	(78.9)	183.4	37.6
Net profit (adj.)	69.5	(60.0)	31.0	37.6
EPS	(8.6)	(78.9)	183.4	37.6
<b>Leverage</b>				
Debt to total capital	9.0	12.2	10.3	0.0
Debt to equity	19.1	23.9	22.1	20.0
Net debt/(cash) to equity	(20.6)	(19.0)	(21.8)	(25.7)
Interest cover (x)	12.5	5.8	7.7	12.1

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