

Earnings call takeaways

Quick Note

Chinasoft hosted its 1H22 post earnings call on 30 August 2022. Management discussed its mid-to-long term plans from cornerstone business to cloud intelligent business, as well as future potential development trend. We believe the company has a clear target to further develop its existing businesses, and is actively seeking new business opportunities to deliver earnings growth. Although we think the company may continue to face some short-term pressure on margins and earnings growth, we expect Chinasoft to further enhance its market position in China and the global IT service market.

We think that investors may have concerns on Chinasoft post the comments from Huawei's (unlisted) founder Mr. Ren, made in the past week (*news*); however, we believe the concerns might be overdone. Looking at Huawei's latest business developments, we note that Huawei established its third batch of "legions" in May 2022 and currently has up to 20 "legions" or integrated teams targeting different business aspects (*news*). Meanwhile, Huawei also unveiled its Multi-domain collaborative, Efficient, Green, and Autonomous (MEGA) financial digital infrastructure in Jul 22 (*news*). Based on Huawei's recent active business developments and our cross-checks, we believe the main purpose of Mr. Ren's comments was to alert the company's staff to remain cautious in developing the new business and focus more on profitability rather than scale. Moreover, we do not see or expect any major change to Huawei's short-term business strategy that may have any negative impact on Chinasoft.

With Chinasoft's share price approaching its historical low valuation level, and considering its relatively healthy 1H22 results (based on Huawei's situation, the macro environment and some COVID-19 impact), we expect limited downward risk on valuation. Should there be any recovery in the market situation or any catalyst appears in Chinasoft's business development ahead, we believe valuation recovery could be easy. We maintain our Buy rating and TP of HKD9.9. Chinasoft is trading at 10x 2023F EPS.

Cornerstone business: Stay in the game and further enhance market position

While Huawei continues to be its strategic customer, the company has also developed other key focused customers in the past few years, e.g. China Mobile (941 HK). As of 1H22, the company has more than 190 customers with revenue contribution of more than CNY6mn each, and the number of such customers has increased by more than 40 on a y-y basis. Meanwhile, Chinasoft noted the concentration rate of its Top5/Top10 customers' revenue contribution declined slightly in 1H22, showing a healthy business development trend. Going forward, the company plans to continue to work closely with key customers to increase its market share (and hence enhance its market position), while continuing to improve its working and operating efficiency to ensure earnings growth at the same time.

Cloud intelligent business and new business: Full-stack cloud service + HarmonyOS ecosystem business + intelligent vehicle

On cloud service, management stated that the company will continue to follow Huawei's cloud business; it hopes to continue to have a 10% share from Huawei cloud, and help its customers with cloud consulting, implementation and management services. Meanwhile, Chinasoft plans to work closely with mainstream cloud players (e.g. Alibaba, BABA US; China Telecom, 728 HK; Kingdee, 268 HK; Yongyou, 600588 CH) and provide full-stack services, including SaaS service, such as CRM from Fxiaohe (unlisted) and MEGA ERP from Huawei, through its Huaxia Cloud platform (one-stop cloud brokerage platform). According to management, the number of its partners for cloud service has increased from 3,000 to 5,000 on a y-y basis. With capability and products improvement, Chinasoft

Rating Remains	Buy
Target price Remains	HKD 9.90
Closing price 30 August 2022	HKD 6.21

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targets to achieve margin improvement for its cloud service business in the long run.

For HarmonyOS and OpenHarmony related businesses, management stated that the company is one of the key contributors to their ecosystems. With a rising independent and controllable technology trend and support from local governments (see [our note](#) published earlier), the company plans to continue to follow Huawei's steps in exploring new business opportunities in the market.

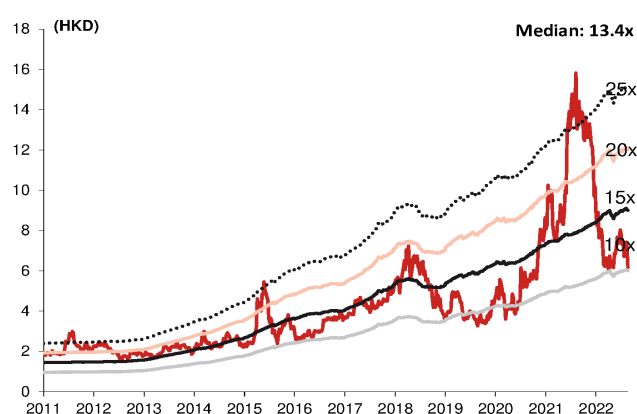
Finally, observing a strong trend in the intelligent vehicle market, the company is actively cooperating with car OEMs (e.g. BYD, 1211 HK) and delivering solid growth in the related business. Its long term target is to provide full-stack turnkey solution of software updates for those car OEMs, including providing digitalization transformation platform for car OEMs, software factory capability and maybe eventually software/OS for intelligent vehicles directly.

Fig. 1: The three growth curve for Chinasoft



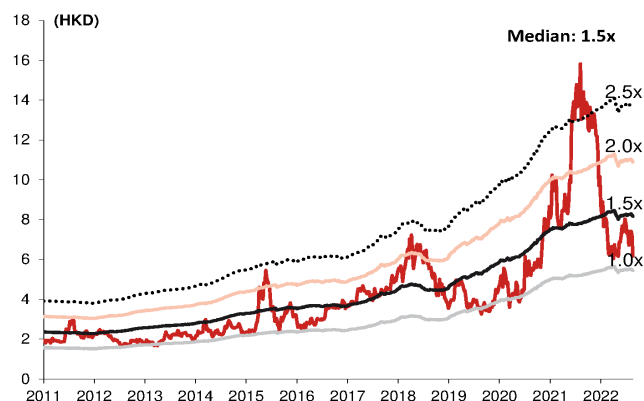
Source: Company data, Nomura research

Fig. 2: Chinasoft: 12-month-forward P/E band



Source: Company data, Bloomberg Finance L.P., Nomura estimates

Fig. 3: Chinasoft: 12-month-forward P/B band



Source: Company data, Bloomberg Finance L.P., Nomura estimates

Appendix A-1

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Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Chinasoft International	354 HK	HKD 6.21	30-Aug-2022	Buy	N/A	

Chinasoft International (354 HK)

HKD 6.21 (30-Aug-2022) Buy (Sector rating: N/A)

Rating and target price chart (three year history)

Chinasoft International

As of 30-Aug-2022
Currency = HKD

Date	Rating	Target price	Closing price
23-May-22	Buy		6.89
23-May-22		9.90	6.89



Source: ThomsonReuters, Nomura research

For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology Our TP of HKD9.90 is based on 16x 2023F EPS of CNY0.53. The target multiple we use is above its historical average, which is below our 2021-24F earnings CAGR of 21% for Chinasoft. The benchmark index for this stock is HSI Index.

Risks that may impede the achievement of the target price Downside risks include: 1) slower-than-expected cornerstone business expansion with key customers due to the loss of wallet share or slower growth rate from key customers; 2) slower-than-expected development of cloud intelligent business due to market competition or self-development issue; and 3) lower-than-expected operating efficiency which has a negative impact on the company's profitability.

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