

Chinasoft Intl (0354.HK): Mgmt. call: Cloud-based IT services to support 2024; Growing focus on Harmony OS, ERP, and AIGC

We hosted Chinasoft Intl. mgmt. at our China Software Day. Overall, management expects the company to achieve double digit YoY revenues growth in 2024, and views cloud-based IT services as a key driver to offset the impact from slower traditional IT services. The company is accelerating Huawei Cloud related software solution and services, along with innovative business across Harmony OS (vertical application, OS migration), ERP localization and AIGC potential opportunities (AI integrated solution, computing power operation services) with better demand, also carrying a higher GM than traditional IT services. Maintain Buy.

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Key takeaways

- **2024 outlook:** Management expects to see 2024 revenues growth at double digit YoY (vs. GSe revenues growth at -5% YoY in 2023) driven by (1) strong growth of Huawei Cloud related software development/ consulting; (2) new drivers across ERP, Harmony OS, AIGC, etc.; and (3) stabilization of traditional IT services.
- **Migration towards cloud-based IT services:** Chinasoft Intl. is shifting more focus to cloud-based services amid macro uncertainties, and expects strong growth of Huawei Cloud related business at over 50% YoY, supported by Huawei Cloud penetration and growing product offering (for example, Database, ERP) on Huawei Cloud.
- **GM outlook:** Management expected improving GM in 2024 mainly driven by product mix upgrade towards cloud-based IT services, and noted GM of traditional IT services taking time to recover. During economy downturns, mgmt. noted GM of traditional IT services comes under pressure due to clients' constraint budget.
- **Harmony OS opportunities:** Chinasoft Intl. and SZ Kai Hong continues to partner with vertical customers on Harmony OS solutions across energy, smart city ([Link](#)) etc.; management also highlighted opportunities of Harmony Next OS targeting to launch by end of 2024, and that Chinasoft Intl. is helping thousands of SMB application vendors migrate to the Harmony OS ecosystem.
- **ERP localization:** Management expects revenues from ERP IT services for Yonyou/ Kingdee/ SAP to reach Rmb600m in 2024E (vs. ~Rmb300m in 2023), driven by better demand and market share gains from global-tier service

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providers (Deloitte, Accenture, KPMG etc.). For MetaERP, mgmt. noted the company is working with clients on product verification and expects to see more rev contribution from 2025.

- **Partnership with Huakin Zhenyu on integration AI platform:** For AI integrated solution covering both hardware and full-stack software solution, management noted Chinasoft Intl. is focused on the software part, thus cooperating with Huakin Zhenyu on the hardware part to offer total solutions for clients.
- **LLM/AIGC services for AI computing platform:** Chinasoft Intl. is cooperating with Huawei on local government's AI/LLM projects (for example, SuZhou project) to offer computing power operation services, and management expects to see strong growth in 2024 on new project wins.
- **Stabilization of traditional IT services:** Management expects to see single digit YoY growth of traditional IT services for Huawei and financial clients amid the challenging macro, and the company continues to see new demand from SOE clients.
- **Headcount expansion:** Mgmt. noted the number of traditional IT services employees depends on client demand, and the company continues to adjust the scale; For the innovative business, management expects the company to allocate more resources to Harmony OS related products for vertical applications and OS migration.

Price Target Risks and Methodology - Chinasoft Intl

Valuation: We have a Buy rating on Chinasoft Intl. with a 12m target price of HK\$7.8 (based on a 15.6x 2024E P/E). We derive our target P/E multiple from its historical trading range. The 15.6x is set in line with its avg. P/E in 2018-2020, when the company enjoyed accelerating earnings growth in 2019-2021, similar to what we expect for the coming 2024E-25E. The 15.6x is also consistent with peer iSoftstone's recent trading average in past 6 months (16.1x).

Key downside risks: 1) Slower-than-expected diversification of customer base; 2) Stronger-than-expected competition; 3) Slower-than-expected investments in R&D; 4) Slower-than-expected product mix upgrade; 5) Lower-than-expected software spending.

0354.HK

12m Price Target: **HK\$7.80**Price: **HK\$4.60**Upside: **69.6%****Buy****GS Forecast**

	12/22	12/23E	12/24E	12/25E	
Market cap: HK\$13.4bn / \$1.7bn	Revenue (Rmb mn)	20,005.2	18,971.2	24,411.8	29,370.4
Enterprise value:	EBITDA (Rmb mn)	1,000.1	1,108.0	1,696.6	2,641.9
HK\$9.8bn / \$1.3bn	EPS (Rmb)	0.26	0.27	0.48	0.78
3m ADTV: HK\$124.7mn / \$16.0mn	P/E (X)	22.3	15.5	8.8	5.4
China	P/B (X)	1.4	0.9	0.9	0.7
Greater China Technology	Dividend yield (%)	0.5	0.7	1.2	1.9
M&A Rank: 3	N debt/EBITDA (ex lease,X)	(3.1)	(2.9)	(1.5)	(1.6)
Leases incl. in net debt & EV?: No	CROCI (%)	9.8	8.0	11.1	15.1
	FCF yield (%)	3.3	2.2	(5.3)	15.8
		6/23	12/23E	6/24E	12/24E
	EPS (Rmb)	0.12	0.15	0.22	0.26

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 7 Feb 2024 close.

Disclosure Appendix

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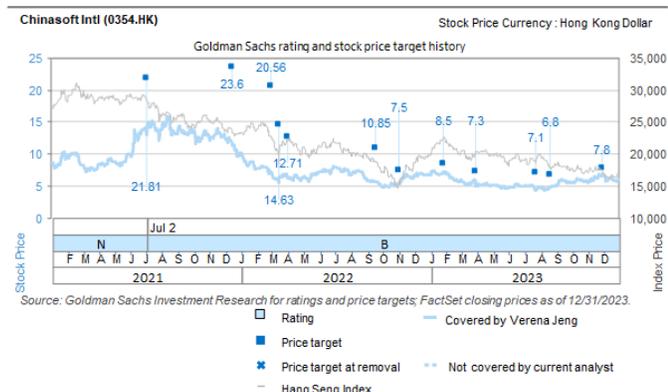
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