

Hon Hai Precision Industry (2317 TT)

 Target price: **TWD145.00** (from TWD145.00)

 Share price (12 May): **TWD102.00** | Up/downside: **+42.2%**

5 4 3 2 1


Buy
 (unchanged)

Solid outlook, attractive valuation and upside in EVs

- 1Q22 operating results beat; solid outlook for 2022
- Management confident on 2022, EV progress, long-term margin trends
- Reiterating our Buy (1) rating and TP of TWD145; a top sector pick

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What's new: Hon Hai's solid 1Q22 results and Chairman Young-Way Liu's confident tone on 2022, the progress in EVs and margin uptrends reaffirm our positive thesis (see [our report](#), 16 March). At a 9.4x 2022E PER, we see its risk-reward as attractive. We reaffirm our Buy (1) call and it remains a top sector pick.

What's the impact: 1Q22 operating results beat. Hon Hai's 1Q22 revenue arrived at TWD1,408bn (-26% QoQ, +4% YoY), above our and market estimates by 3-6%. With a better gross margin on scale benefits and favourable forex, and solid opex control, the operating margin arrived at 2.6% (vs 2.0% in 1Q21) with operating profit of TWD36.7bn (-30% QoQ, +33% YoY), ahead our and street estimates by 20-30%. Due to lower non-op gains on financial market volatility, 1Q22 net profit was TWD29.5bn (-34% QoQ; +5% YoY), in line with our and street estimates.

Solid 2Q22 outlook. Hon Hai reiterated its confident tone for 2Q22, expecting relatively flat revenue YoY/QoQ with growth in cloud, computing, and components except smartphones given a high base. On strong execution offsetting extra costs from the pandemic overhang, we expect it to maintain its operating margin at 2.6% in 2Q22 (vs. 2.6% in 1Q22).

Confident on 2022 with better visibility; optimistic on EVs and long-term margin trends. Despite the demand uncertainty and pandemic overhang, the chairman was confident on the 2022 earnings growth target. He sees visibility improving with strong growth in servers/CSP and components on share gains and expects computing product revenue to grow YoY (vs. relatively flat previously). For EVs, he sees the progress as on track; the company has acquired its first US production site (see [JV with Lordstown](#), 12 May). On an improving mix with rising contribution from EVs, semi, and key components, Hon Hai is confident of reaching its 10% gross margin target in 2025. Hon Hai also shared its long-term ESG targets and recent progress in ESG (see page 6). The chairman's confident tone for 2022 and the EV business reaffirms our positive view, and we believe Hon Hai's efforts on ESG will offer further rerating opportunities. Overall, we forecast Hon Hai to record 12-19% YoY operating profit growth over 2022-23 and see upside in EVs, which we have not factored into our forecasts.

What we recommend: We keep our 2022-23 EPS roughly unchanged. We reaffirm our Buy (1) call and TP of TWD145, based on 13x PER on our 1-year forward EPS forecast. Risk: greater pricing competition.

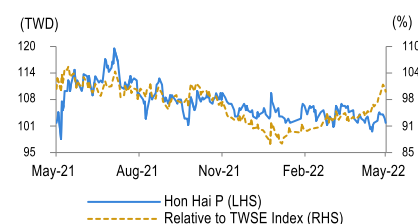
How we differ: Our 2023E EPS is 6% above the consensus, likely due to our more optimistic view on benefits from its transformation plan.

Forecast revisions (%)

Year to 31 Dec	22E	23E	24E
Revenue change	0.2	-	n.a.
Net profit change	0.2	-	n.a.
Core EPS (FD) change	0.2	-	n.a.

Source: Daiwa forecasts

Share price performance



12-month range	98.20-119.50
Market cap (USDbn)	47.62
3m avg daily turnover (USDm)	90.48
Shares outstanding (m)	13,863
Major shareholder	Terry Gou (12.6%)

Financial summary (TWD)

Year to 31 Dec	22E	23E	24E
Revenue (m)	6,260,000	6,500,000	6,720,000
Operating profit (m)	177,158	197,600	218,400
Net profit (m)	150,456	173,426	189,307
Core EPS (fully-diluted)	10.853	12.510	13.656
EPS change (%)	8.0	15.3	9.2
Daiwa vs Cons. EPS (%)	2.2	6.4	8.8
PER (x)	9.4	8.2	7.5
Dividend yield (%)	5.1	5.1	4.4
DPS	5.2	5.2	4.5
PBR (x)	1.0	0.9	0.8
EV/EBITDA (x)	4.6	4.0	3.3
ROE (%)	10.6	11.5	11.7

Source: FactSet, Daiwa forecasts

Financial summary

Key assumptions

PC and networking related sales growth (YoY%)	3.4	3.6	5.1	11.5	6.1	7.3	11.6	10.0
iPhone shipment (mn units)	153.0	140.2	129.1	133.5	165.0	173.7	167.3	164.5
iPad shipment (mn units)	37.9	38.1	44.0	43.0	48.5	46.1	43.8	41.6

Profit and loss (TWDm)

Year to 31 Dec	2017	2018	2019	2020	2021	2022E	2023E	2024E
PC/NB/networking Revenues	1,229,625	1,269,831	1,331,019	1,482,853	1,572,401	1,686,138	1,880,794	2,068,214
Mobile Device Revenues	2,694,077	2,916,938	2,811,402	2,708,250	3,335,442	3,488,651	3,384,373	3,319,458
Other Revenue	783,035	1,107,034	1,200,389	1,166,920	1,086,331	1,085,211	1,234,833	1,332,328
Total Revenue	4,706,736	5,293,803	5,342,811	5,358,023	5,994,174	6,260,000	6,500,000	6,720,000
Other income	0	0	0	0	0	0	0	0
COGS	(4,403,729)	(4,961,773)	(5,026,943)	(5,055,104)	(5,632,047)	(5,863,742)	(6,064,500)	(6,259,680)
SG&A	(108,655)	(111,453)	(109,423)	(97,981)	(108,099)	(142,415)	(154,635)	(157,248)
Other op.expenses	(81,781)	(84,430)	(91,548)	(94,111)	(105,069)	(76,685)	(83,265)	(84,672)
Operating profit	112,570	136,147	114,897	110,827	148,959	177,158	197,600	218,400
Net-interest inc./(exp.)	7,311	4,856	9,219	7,617	10,498	1,619	2,868	4,323
Assoc/forex/extraord./others	62,991	29,249	39,762	27,027	34,115	24,332	31,717	32,096
Pre-tax profit	182,873	170,251	163,878	145,472	193,572	203,109	232,185	254,819
Tax	(47,498)	(40,416)	(31,693)	(31,147)	(39,749)	(42,653)	(48,759)	(53,512)
Min. int./pref. div./others	3,360	(770)	(16,876)	(12,531)	(14,503)	(10,000)	(10,000)	(12,000)
Net profit (reported)	138,734	129,065	115,309	101,795	139,320	150,456	173,426	189,307
Net profit (adjusted)	138,734	129,065	115,309	101,795	139,320	150,456	173,426	189,307
EPS (reported)(TWD)	8.006	8.033	8.318	7.343	10.050	10.853	12.510	13.656
EPS (adjusted)(TWD)	8.006	8.033	8.318	7.343	10.050	10.853	12.510	13.656
EPS (adjusted fully-diluted)(TWD)	8.006	8.033	8.318	7.343	10.050	10.853	12.510	13.656
DPS (TWD)	4.500	2.157	4.000	4.200	4.000	5.200	5.200	4.500
EBIT	112,570	136,147	114,897	110,827	148,959	177,158	197,600	218,400
EBITDA	173,571	196,073	181,906	175,941	224,441	251,658	283,100	315,900

Cash flow (TWDm)

Year to 31 Dec	2017	2018	2019	2020	2021	2022E	2023E	2024E
Profit before tax	182,873	170,251	163,878	145,472	193,572	203,109	232,185	254,819
Depreciation and amortisation	59,737	58,211	65,144	60,952	70,125	74,500	85,500	97,500
Tax paid	(47,498)	(40,416)	(31,693)	(31,147)	(39,749)	(42,653)	(48,759)	(53,512)
Change in working capital	(262,468)	(45,155)	121,066	233,660	(304,213)	(2,912)	(22,390)	(19,705)
Other operational CF items	(10,817)	(16,232)	(19,634)	(9,212)	(18,405)	(8,564)	(8,411)	(8,224)
Cash flow from operations	(78,174)	126,659	298,761	399,726	(98,669)	223,480	238,125	270,877
Capex	(50,390)	(37,649)	(70,951)	(59,395)	(84,527)	(110,000)	(120,000)	(120,000)
Net (acquisitions)/disposals	25,066	(22,607)	3,189	(29,564)	(35,371)	0	0	0
Other investing CF items	(25,099)	2,770	(51,989)	(9,320)	(22,014)	(3,634)	(3,716)	(3,800)
Cash flow from investing	(50,423)	(57,486)	(119,751)	(98,279)	(141,911)	(113,634)	(123,716)	(123,800)
Change in debt	263,238	150,420	(34,541)	115,224	136,484	31,656	32,555	33,480
Net share issues/(repurchases)	0	0	0	0	0	0	0	0
Dividends paid	(77,979)	(34,657)	(55,452)	(58,225)	(55,452)	(72,088)	(72,088)	(62,383)
Other financing CF items	(55,284)	33,250	(31,751)	13,723	(688)	0	0	0
Cash flow from financing	129,975	149,012	(121,744)	70,723	80,343	(40,432)	(39,533)	(28,904)
Forex effect/others	0	0	0	0	0	0	0	0
Change in cash	1,378	218,185	57,267	372,169	(160,237)	69,414	74,876	118,174
Free cash flow	(128,564)	89,010	227,810	340,330	(183,196)	113,480	118,125	150,877

Source: FactSet, Daiwa forecasts

Financial summary continued ...

Balance sheet (TWDm)

Year to 31 Dec	2017	2018	2019	2020	2021	2022E	2023E	2024E
Cash & short-term investment	654,860	873,990	916,245	1,280,045	1,110,661	1,170,075	1,234,951	1,341,125
Inventory	560,955	625,026	515,772	582,114	672,145	689,852	713,471	736,433
Accounts receivable	1,229,237	1,057,175	1,031,840	942,484	1,161,219	1,200,548	1,246,575	1,288,767
Other current assets	301,084	150,292	109,836	80,006	90,393	94,401	98,020	101,338
Total current assets	2,746,136	2,706,483	2,573,693	2,884,649	3,034,417	3,154,876	3,293,018	3,467,663
Fixed assets	278,204	277,860	287,523	287,092	310,107	346,546	382,014	405,510
Goodwill & intangibles	0	0	0	0	0	0	0	0
Other non-current assets	382,876	397,013	459,726	502,534	564,354	575,613	586,773	597,801
Total assets	3,407,217	3,381,355	3,320,942	3,674,276	3,908,878	4,077,036	4,261,804	4,470,974
Short-term debt	474,618	562,916	464,495	542,474	608,958	547,666	564,096	581,018
Accounts payable	1,216,485	948,023	906,188	1,065,593	1,076,178	1,120,451	1,158,812	1,196,107
Other current liabilities	334,399	298,922	286,779	308,191	312,544	326,405	338,919	350,390
Total current liabilities	2,025,502	1,809,862	1,657,461	1,916,257	1,997,680	1,994,521	2,061,826	2,127,515
Long-term debt	190,147	216,719	217,082	234,978	277,232	365,110	376,064	387,346
Other non-current liabilities	107,347	142,897	206,414	225,763	253,508	258,579	263,750	269,025
Total liabilities	2,322,996	2,169,477	2,080,957	2,376,998	2,528,421	2,618,210	2,701,640	2,783,886
Share capital	173,287	138,630	138,630	138,630	138,630	138,630	138,630	138,630
Reserves/R.E./others	910,933	1,073,249	1,101,354	1,158,647	1,241,827	1,320,196	1,421,534	1,548,458
Shareholders' equity	1,084,221	1,211,878	1,239,984	1,297,277	1,380,457	1,458,826	1,560,164	1,687,088
Minority interests	0	0	0	0	0	0	0	0
Total equity & liabilities	3,407,217	3,381,355	3,320,942	3,674,276	3,908,878	4,077,036	4,261,804	4,470,974
EV	1,423,931	1,319,670	1,179,356	911,432	1,189,555	1,156,726	1,119,233	1,041,264
Net debt/(cash)	9,905	(94,355)	(234,669)	(502,593)	(224,471)	(257,299)	(294,792)	(372,761)
BVPS (TWD)	62.568	87.418	89.446	93.578	99.579	105.232	112.542	121.697

Key ratios (%)

Year to 31 Dec	2017	2018	2019	2020	2021	2022E	2023E	2024E
Sales (YoY)	8.0	12.5	0.9	0.3	11.9	4.4	3.8	3.4
EBITDA (YoY)	(27.1)	13.0	(7.2)	(3.3)	27.6	12.1	12.5	11.6
Operating profit (YoY)	(35.7)	20.9	(15.6)	(3.5)	34.4	18.9	11.5	10.5
Net profit (YoY)	(6.7)	(7.0)	(10.7)	(11.7)	36.9	8.0	15.3	9.2
Core EPS (fully-diluted) (YoY)	(6.7)	0.3	3.5	(11.7)	36.9	8.0	15.3	9.2
Gross-profit margin	6.4	6.3	5.9	5.7	6.0	6.3	6.7	6.9
EBITDA margin	3.7	3.7	3.4	3.3	3.7	4.0	4.4	4.7
Operating-profit margin	2.4	2.6	2.2	2.1	2.5	2.8	3.0	3.3
Net profit margin	2.9	2.4	2.2	1.9	2.3	2.4	2.7	2.8
ROAE	12.8	11.2	9.4	8.0	10.4	10.6	11.5	11.7
ROAA	4.6	3.8	3.4	2.9	3.7	3.8	4.2	4.3
ROCE	6.9	7.3	5.9	5.5	6.9	7.6	8.1	8.5
ROIC	8.5	9.4	8.7	9.7	12.1	11.9	12.7	13.4
Net debt to equity	0.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Effective tax rate	26.0	23.7	19.3	21.4	20.5	21.0	21.0	21.0
Accounts receivable (days)	75.9	78.8	71.4	67.2	64.0	68.9	68.7	68.9
Current ratio (x)	1.4	1.5	1.6	1.5	1.5	1.6	1.6	1.6
Net interest cover (x)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Net dividend payout	25.0	43.0	50.5	54.5	51.7	47.9	36.0	33.0
Free cash flow yield	n.a.	6.3	16.1	24.1	n.a.	8.0	8.4	10.7

Source: FactSet, Daiwa forecasts

Company profile

Established in 1974, Hon Hai Precision Industry (Hon Hai) started out making plastic products, connector products and cable assemblies. It is now the largest electronics manufacturing service (EMS) provider globally in terms of design, manufacturing, global logistics and after-market service.

Business update

1Q22 operating results a solid beat

Hon Hai's 1Q22 revenue arrived at TWD1,408bn (-26% QoQ, +4% YoY), above our and market estimates by 3-6%, likely mainly driven by strong iPhone shipments (see [our memo](#), 6 April). On scale benefits and a favourable mix, Hon Hai's gross margin arrived at 6.0% (vs. 6.0% in 4Q21; 5.8% in 1Q21), slightly ahead of our/street estimates of 5.9-6.0%. On solid opex control, operating profit arrived at TWD36.7bn (-30% QoQ, +33% YoY) with an operating margin of 2.6% (vs. 2.8% in 4Q21 and 2.0% in 1Q21), ahead of our and street estimates by 20-30%. Due to lower non-op gains on lower investment income on financial market volatility, 1Q22 net profit was TWD29.5bn (-34% QoQ; +5% YoY) with EPS of TWD2.1, was in line with our and street estimates.

Solid 2Q22 outlook

Hon Hai reiterated its confident tone for 2Q22, expecting relatively flat revenue YoY/QoQ on growth in cloud, computing, and components, except for smartphones which is expected to decline on a high base and a transition period for new and old products. For the cloud business, thanks to strong server demand, especially rapid growth in CSP clients, Hon Hai expects the business to see strong revenue growth. For the computing business, despite being affected by the pandemic, the company expects to make use of its supply chain management advantages to secure growth. For its components business, it expects to benefit from market share gains and sees revenue growth despite shipments being impacted by the pandemic. On strong execution capability offsetting extra costs due to the pandemic, we expect Hon Hai maintain its operating margin at 2.6% in 2Q22 (vs. 2.6% in 1Q22).

In total, the company is expecting relatively flat revenue YoY/QoQ, and we forecast Hon Hai to maintain its operating margin at 2.6% in 2Q22 on strong execution capability, offsetting the extra costs due to the pandemic

Management confident for 2022; solid progress in new business – EVs and semi

Looking ahead, despite the demand uncertainty and pandemic overhang, the chairman is confident on the company's 2022 earnings growth target. He sees visibility improving with strong demand in the server market, especially from CSP clients, and also mentioned that there are possibilities for it to further acquire market share in this segment. For computing products, Hon Hai expects YoY revenue growth in 2022 (vs. relatively flat previously), thanks to increased end demand and market share gains. For its components business, Hon Hai maintained its positive view as it continues to gain market share.

For EVs, the chairman views the progress as on track. Hon Hai highlighted its target to reach TWD1,000bn of revenue (500-750k annual shipments) by 2025, and its solid development in EVs. It also highlighted its strategy to continue to expand its client base from Taiwan, the US, and Southeast Asia to Europe and other Asian countries. On recent progress in its EV business, Hon Hai highlighted the signing of a contract manufacturing agreement, a joint venture agreement for product development with Lordstown Motors (RIDE US) on 12 May. It will invest USD55m in the new joint venture and hold a 55% stake in the joint venture, MIH EV Design LLC, which will design new EV models based on its MIH platform. Hon Hai also announced the completion of the facility purchase of Lordstown's production plant in Ohio, which is a follow-up to the announcement on 1 October 2021 of its plan to acquire Lordstown's Ohio plant for USD230m (see [Cooperation with Lordstown Motor – a milestone for EV manufacturing in the US](#), 1 October 2021). The production site will be the first US production site for Hon Hai, while Lordstown will become its first mass-produced commercial vehicle client. Hon Hai will start manufacturing Lordstown's electric pickup truck from 2H22 (see [JV with Lordstown – another solid progress in EV development](#), 12 May 2022). Hon Hai also highlighted other progress, including its Thailand plant cooperation with PTT (see [JV with PTT – a milestone for EV development in ASEAN market](#), 14 September 2021), which is expected to be completed at the end of 2023 and enter production in 2024, the introduction of its Model T in Taipei

City in March 2022, and plans to collaborate with Microsoft to advance AI technology in the EV and digital health market.

For semiconductors, the company plans to build a comprehensive ecosystem, ranging from upstream design, wafer manufacturing and power module to downstream application, by cooperating with other companies and building its own capacities. LiDAR is another important step for Hon Hai. It will continue to complete LiDAR vertical integration through developing LiDAR total solutions based on hardware and software integration, and highlighted that it will have a competitive advantage in terms of specifications and cost. Hon Hai acquired arQana's wireless telecommunication business in April 2022 to expand its footprint in the semiconductor business.

Hon Hai is confident it will reach its 10% gross margin target in 2025

Due to an improving mix with rising contribution from EVs, semi, and key components, Hon Hai is confident of reaching its 10% gross margin target in 2025. The chairman's confident tone for 2022 and its EV business reaffirms our positive view (see [Solid outlook, attractive valuation and upside in EV](#), 16 March), and we believe its efforts in ESG will offer further rerating opportunities. Overall, we forecast Hon Hai to record 12-19% YoY operating profit growth over 2022-23 and see upside in EVs, which we have not factored into our forecasts.

Hon Hai: development in EV/auto and other fields

Date	Details
16/1/2020	Announced that it will form a JV with Fiat Chrysler Automobile (FCA), focusing on NEVs
7/2/2020	Announced that it will form a JV with Yulon Motor's fully-owned subsidiary HAITAC, targeting to leverage its experience in car model development
16/10/2020	Introduced MIH platform during HHTD, which will be an open platform with a variety of product offerings in software and hardware; Hon Hai targets to be the "Android of EV"
12/11/2020	Announced that AWS, CATL, Microsoft, TI, Qualcomm, Mediatek, ROHM, and ST have shown interest in its MIH platform
20/12/2020	Announced that DANA, EATON, CarOTA, Tier IV, Autocore and ADLINK have joined its MIH platform
27/12/2021	Announced that DEPO has joined its MIH platform, which will strengthen MIH's technology on auto lamps
4/1/2021	Announced its strategic partnership with Byton and Nanjing Development Zone, targeting to accelerate production of Byton's Mbyte by 1Q22 as part of Hon Hai's 3+3 vision
13/1/2021	Announced that it will set up a JV with Geely; the JV aims to offer global automotive and ridesharing companies total EV solutions; Hon Hai believes that with its manufacturing capabilities and Geely's expertise in auto, they can provide a competitive design and manufacturing platform
28/1/2021	Geely announced cooperation with Faraday Future (FF); Geely and Foxconn will provide OEM production manufacturing services to FF and technology/engineering support
31/1/2021	Launched its EV Kit that provides autonomous driving developers with an easily accessible platform that can shorten the time for system design and verification via open communication protocols and drive-by-wire technology; the sample will first be used in the Luxgen Motor S3 U5; Hon Hai also announced that it will hold its first EV Kit member gathering in March and claimed to have 500+ members
20/2/2021	Announced the launch of 3 EV models with MIH reference design in 4Q21 (one e-bus and two commercial EVs) and claimed to have 746 members on the MIH platform; expects to see the EV boom advance to 2024 and targets to have a 10% market share by 2025
24/2/2021	Announced its cooperation with Fisker (FSR US) to launch an EV model under project PEAR; they plan to enter mass production by 4Q23 and targets to ship more than 250,000 vehicles annually
1/3/2021	Announced investment in autonomous driving start-up Autocore.ai's pre-A round with GL Ventures as lead investors; the cooperation could enhance its technology in autonomous driving applications
18/3/2021	Announced signing of MOU with Nidec (6594 JP); with Nidec's strength in e-powertrain and Foxtron's vehicle design and engineering capability, the move will strengthen the capability of the MIH platform; they will work on both passenger and commercial vehicles
25/3/2021	MIH held its first member conference; it now has over 1,200 members (90% hardware and 10% software suppliers); it targets to introduce an electric bus in 2022 and mass-produce C-Class EVs in 2023
5/5/2021	Hon Hai and Yageo (2327 TT) announced the formation of a semiconductor JV, Xsemi Corporation, to work on product development and sales of small ICs; the company can help provide stable IC supply to EV clients
14/5/2021	Announced on-track progress with Fisker; targets to enter mass production in 4Q23 by providing whole-car manufacturing and components (small ICs, display, e-powertrain); first manufacturing site will be in the US
18/5/2021	Hon Hai, together with FIH, announced the signing of an MOU with Stellantis (STLA MI) to form a 50:50 JV, Mobile Drive, which targets to speed up the development timeline of smart cars with innovative in-vehicle user experience
31/5/2021	Announced the signing of an MOU with PTT (PTT TB) to form an open EV platform, aimed at providing comprehensive EV manufacturing services to Thailand's auto makers and to accelerate the development timeline; the platform will target the ASEAN market
10/6/2021	Announced that it will spend MYR108m (TWD726m) to obtain 5.0% stake in Dagang Nexchange Berhad (DNEX); DNEX is the major shareholder of Silterra, which is an 8-inch semi foundry; Hon Hai believes the cooperation will strengthen its capability in semiconductors
15/6/2021	Announced its investment of TWD995m to obtain a 10.5% stake in Giga Solar (3691 TT) to co-develop EV battery materials and accelerate key component offerings for global EV markets
23/6/2021	Announced the signing of an MOU with Gogoro to accelerate the development of Gogoro's battery swapping system and smart scooter
6/7/2021	Foxtron announced the signing of an MOU with San-Ti Group's North-Star International Company (8927 TT) and Kaohsiung Bus Company; both parties will co-develop the e-bus based on the MIH commercial vehicle platform and target to start operations in 2022
14/7/2021	Announced its participation in the SES PIPE deal to cooperate in the next-generation lithium-metal EV battery technology development
16/7/2021	Announced the signing of an MOU with CTBC FHC (2891 TT) to establish an EV industry fund to invest in Taiwanese companies; they target to raise TWD5-10bn in total
21/7/2021	Hon Hai and Foxtron plan to form a JV with Nidec (6594 JP) in Taiwan to work on development, production and sales of traction motors; they target to establish the JV in 2022
5/8/2021	Announced that it will spend TWD2.52bn to purchase a 6-inch wafer fab from Macronix (2337 TT); the fab will focus on R&D and mass production of third-generation semiconductors, especially SiC for EVs; targets monthly capacity of 15k wafers by 2024
24/8/2021	Announced that FIH and Stellantis will each hold 50% of Mobile Drive. Stellantis will contribute USD40m (in EUR) to the JV and grant license of mutually agreed IP while FIH will contribute mutually agreed business and assets of Mobile Drive Taiwan and Mobile Drive China
14/9/2021	Announced it will set up a JV with PTT (PTT TB). The total investment amount will be around USD1-2bn and they will start with setting up a plant for whole car manufacturing. In terms of capacity, they target initial capacity of 50k annually by 2023 and expect to gradually ramp up to 150k in the future
28/9/2021	Announced signing of MOU with CSCC (1723 TT), Giga Solar (3691 TT), and Long Time Tech (6555 TT) to co-develop EV battery. Hon Hai targets to unveil its first e-Bus battery by 2023
1/10/2021	Announced reaching agreement with Lordstown Motor (RIDE US) on EV manufacturing and assembly. It targets to spend USD230m to purchase Lordstown's facilities and aims to sign a manufacturing contract for Lordstown's Endurance all-electricity pickup trucks, targeting mass production by April 2022. Hon Hai will also spend USD50m to obtain 3.8% of Lordstown Motor's shares
18/10/2021	Hon Hai hosted its Hon Hai Tech Day (HHTD) on 18 October and unveiled its first three EV prototypes including a quality SUV, a luxury sedan, and an e-Bus
10/11/2021	Foxconn and Lordstown Motors enter into a strategic partnership
21/1/2022	Hon Hai, Gogoro, IBC and Indika to jointly develop a sustainable new energy ecosystem project in Indonesia through investment cooperation in electric battery, electric vehicles (EV) and its supporting industries
14/2/2022	Vedanta, one of India's leading multinational groups, and Hon Hai Technology Group (Foxconn), the world's largest electronics manufacturing company, announced the signing of an MOU to form a joint venture company that will manufacture semiconductors in India
22/2/2022	Announced its plan to invest USD150m (SAR562.5m) to form an 8.2%-owned JV with Public Investment Fund (Saudi Arabia's Public government fund)
22/2/2022	Announced the signing of an MOU with XRSPACE for the right to invest USD100m in XRSPACE
16/3/2022	Announced its plan to release 2 new EV prototypes in 2H22
13/4/2022	Announced the completion of the acquisition of arQana's wireless telecommunications business
12/5/2022	Announced the signing of a contract manufacturing agreement and joint venture agreement for product development with Lordstown Motors (RIDE US); Hon Hai announced the completion of the purchase of Lordstown's facilities

Source: Company, Daiwa

Strong ESG commitments

Hon Hai also reiterated its goals and commitment to ESG during the investor conference

Besides the business update, Hon Hai also reiterated its goals and commitment to ESG during the investor conference. On the environment, Hon Hai has submitted its application of science-based target setting to the Science Based Targets initiative (SBTi) for assessment. Hon Hai also highlighted its target to reach 100% green energy at its Taiwan offices and 50% green energy usage at its Taiwan sites by 2030, and reiterated its 2050

target to achieve net-zero emissions. On social activities, Hon Hai reiterated its 10 long-term goals to boost employee wellbeing and nurture a positive social environment. The goals include attracting more diverse talent, assuring equal employment opportunities, increasing the professional talent retention rate to 88%, and ensuring no severe labour rights incidents that might damage the reputation of Hon Hai and its clients, among others. On governance, Hon Hai has set up a Nomination Committee to enhance its board composition diversity. For this year’s board member nominees, over half are independent directors, and it has increased its female directors to 2. Hon Hai will also release its goals on governance in the near future.

Hon Hai has received several recognitions, including its headquarters being certified by Fitwel as a health building; its Longhua Campus was awarded the UL 2799 Gold-Level Certification for zero waste as the first ecological demo site, and it will continue to promote the concept of zero waste to other its campuses. It also received the First Place Award within the electronics industry category in the ESG field from Global Views Monthly. Overall, we recognise Hon Hai’s solid commitment to ESG.

Hon Hai: ESG implementation

2022/03/16
Set up Nomination Committee to enhance Board composition diversity

2022/04/15
Purchased green energy from Shinfon Energy and targeted to reach 50% green energy usage at Taiwan sites by 2030

2022/04/22 & 2022/05/06
Revealed Environment, and Social Long-Term goals for ESG

Source: Company

Hon Hai: ESG recognition

2022/03/11
Headquarter, the first building in Taiwan, certified by Fitwel 3-star Award

2022/04/08
Longhua Campus awarded UL 2799 Gold-Level Certification of zero waste as the first ecological demo site

2022/05/03
Received the First Place Award within electronics industry category in ESG field by Global Views Monthly

Source: Company

Valuation and recommendation

Reiterating Buy (1) and maintain 12-month TP at TWD145

We reiterate our Buy (1) rating and maintain the 12-month TP at TWD145, still based on a 13x PER on our revised 1-year forward EPS estimate

The chairman's confident tone for 2022 and the EV business reaffirms our positive view (see [Solid outlook, attractive valuation and upside in EV](#), 16 March), and we believe its efforts in ESG will offer further re-rating opportunities. Looking ahead, we forecast Hon Hai to record 12-19% YoY operating profit growth over 2022-23 and see upside in EVs, which we have not factored into our forecasts.

We keep our 2022-23 EPS roughly unchanged, and introduce our 2024 forecasts. We reaffirm our Buy (1) call and 12-month TP of TWD145, still based on 13x PER on our 1-year forward EPS forecast. The stock is trading at a 9.4x 2022E PER, which we view as attractive.

Risk

Key downside risk to our view on Hon Hai would be higher pricing competition.

Hon Hai: forecast revisions

(TWDm)	Revised forecasts			Previous forecasts			Change		
	2022E	2023E	2024E	2022E	2023E	2024E	2022E	2023E	2024E
Revenues	6,260,000	6,500,000	6,720,000	6,250,000	6,500,000	n.a.	0.2%	0.0%	n.a.
Gross profit	396,258	435,500	460,320	393,125	435,500	n.a.	0.8%	0.0%	n.a.
Operating profit	177,158	197,600	218,400	168,750	196,950	n.a.	5.0%	0.3%	n.a.
Pre-tax profit	203,109	232,185	254,819	209,085	239,709	n.a.	-2.9%	-3.1%	n.a.
Net profit	150,456	173,426	189,307	150,177	173,370	n.a.	0.2%	0.0%	n.a.
EPS (TWD)	10.85	12.51	13.66	10.83	12.51	n.a.	0.2%	0.0%	n.a.
Margins (%)									
Gross Margin	6.3%	6.7%	6.9%	6.3%	6.7%	n.a.			
Operating Margin	2.8%	3.0%	3.3%	2.7%	3.0%	n.a.			
Pre-tax Margin	3.2%	3.6%	3.8%	3.3%	3.7%	n.a.			
Net Margin	2.4%	2.7%	2.8%	2.4%	2.7%	n.a.			

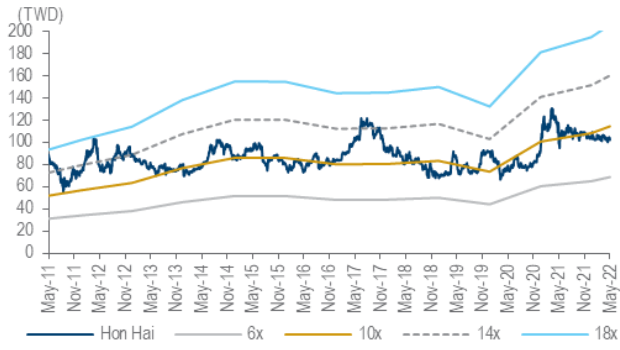
Source: Daiwa forecasts

Hon Hai: quarterly and annual P&L statements

(TWDm)	2022E				2023E				2022E	2023E	2024E
	1Q	2QE	3QE	4QE	1QE	2QE	3QE	4QE			
Net sales	1,407,553	1,389,519	1,499,815	1,963,113	1,459,405	1,473,425	1,570,349	1,996,820	6,260,000	6,500,000	6,720,000
Gross profit	84,766	84,761	97,488	129,243	91,943	94,299	111,495	137,763	396,258	435,500	460,320
Operating costs	48,097	48,633	52,644	69,726	56,333	59,821	57,475	64,271	219,100	237,900	241,920
Operating profit	36,669	36,127	44,844	59,517	35,609	34,478	54,020	73,492	177,158	197,600	218,400
Pretax profit	36,927	42,615	51,023	72,543	43,295	43,124	62,666	83,099	203,109	232,185	254,819
Net profit	29,450	28,609	38,319	54,078	32,197	25,531	47,633	68,065	150,456	173,426	189,307
EPS (TWD)	2.12	2.06	2.76	3.90	2.32	1.84	3.44	4.91	10.85	12.51	13.66
Operating Ratios											
Gross margin	6.0%	6.1%	6.5%	6.6%	6.3%	6.4%	7.1%	6.9%	6.3%	6.7%	6.9%
Operating margin	2.6%	2.6%	3.0%	3.0%	2.4%	2.3%	3.4%	3.7%	2.8%	3.0%	3.3%
Pre-tax margin	2.6%	3.1%	3.4%	3.7%	3.0%	2.9%	4.0%	4.2%	3.2%	3.6%	3.8%
Net margin	2.1%	2.1%	2.6%	2.8%	2.2%	1.7%	3.0%	3.4%	2.4%	2.7%	2.8%
YoY (%)											
Net revenue	4%	3%	7%	4%	4%	6%	5%	2%	4%	4%	3%
Gross profit	8%	4%	10%	14%	8%	11%	14%	7%	9%	10%	6%
Operating income	33%	11%	24%	13%	-3%	-5%	20%	23%	19%	12%	11%
Net income	5%	-4%	4%	22%	9%	-11%	24%	26%	8%	15%	9%
QoQ (%)											
Net revenue	-26%	-1%	8%	31%	-26%	1%	7%	27%			
Gross profit	-26%	0%	15%	33%	-29%	3%	18%	24%			
Operating income	-30%	-1%	24%	33%	-40%	-3%	57%	36%			
Net income	-34%	-3%	34%	41%	-40%	-21%	87%	43%			

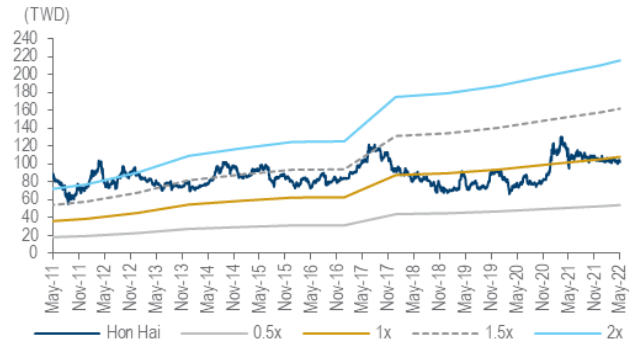
Source: Company, Daiwa forecasts

Hon Hai: 1-year forward PER



Source: Company, Daiwa forecasts

Hon Hai: 1-year forward PBR



Source: Company, Daiwa forecasts

ESG analysis

ESG risks

Risks	Management	Analyst comments	
G	Executive/board quality	2	Hon Hai has incorporated 3 independent members into its 9-people Board of Directors in pursuit of better governance. However, the company's Chairman and CEO are the same person, representing an absence of separation of roles.
	Capital management	1	Hon Hai declared over 40% payout ratio during most of the years since 2014, pointing to a shareholder-friendly dividend policy.
	Related party & transaction	2	Revenue from related parties accounted for 3% of total revenue in 2020, while purchases from related parties were at 2% of cost of sales. The majority of the related-party transactions came from its business with Sharp and its subsidiary. We see limited risk from related-party transactions.
S	Supply chain management	1	Hon Hai aims to integrate sustainability into its supply chain and requires its suppliers to comply with a series of standards rolled out by Hon Hai as well as third-party organisations.
S	Labor practices	2	Hon Hai recognizes employees as the most important asset and continues to invest in its workforce. In 2020, it invested TWD400m in Foxconn University for employee education and TWD176m in its employee baby welfare programme. In terms of safety, Hon Hai has an Emergency Response Centre, aiming to achieve its goals of "100% Safety at Work" and "zero injuries, occupational disease or accidents". Overall, we note that Hon Hai has improved in labour management in recent years.
S	Product design & lifecycle management	2	Hon Hai adhere to green design concepts and incorporate environmental factors and pollution prevention measures during the design and development stages. The company's green product design guidelines include four axes: "energy-saving, non-harmful, reduction and easily recyclable."
Company specific	Management	Analyst comments	
E	GHG emissions	2	Hon Hai announced it will commit to Climate Action 100+ in November 2020 and aims to achieve net-zero greenhouse gas emissions by 2050. Its GHG emission intensity (tonnes/TWDM sales) improved from 1.48 in 2019 to 1.03 in 2020.

Note: Management score represents a company's ability to manage/benefit from certain ESG topics. The scores range from 1 to 3, with 1 being the strongest.

Source: Daiwa

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