

## Hon Hai (2317.TW): Solid 1Q22 revenues growth while 2Q22 to be affected by COVID and soft market demand; Neutral

Hon Hai 1Q22 revenues were solid at +5% YoY, despite the Shenzhen factory site lockdown for around a week, in our view demonstrating the company's strong execution and bargaining power with the supply chain. However, with more regional lockdowns in 2Q22 in China, especially in Shanghai, Kunshan, and Zhengzhou, along with soft consumer electronics market demand, we expect revenue growth in 2Q22 to be lower than 1Q22, at +0% YoY. Although Hon Hai's mega sites production is operating normally under COVID, we expect the logistics and supply chain disruption could still weight on its revenue growth. Note that we continue to expect revenue growth to be better than 1Q20 (-12% YoY) during the initial COVID outbreak in China with a nationwide impact. We believe Hon Hai's strong execution and experience in 2020 could better offset the COVID impact in 2Q22 compared to 2020.

**Earnings revision:** We factor in 1Q22 revenues and thus lift 2022-23E revenues by 5% / 1%. We also newly introduced 2024E estimates, we continue to expect modest revenue growth ahead through 2024E with +0% / -4% / -3% YoY in 2022-24E, considering growing competition in EMS, while its automotive business remains small (0.6% / 1.0% / 1.4% of 2022-24E revenues). We lower our GM estimate to reflect the concerns on growing competition and additional costs due to COVID, and now expect GM to stay at 2021 level of 6.0% in 2022 (albeit still higher than 2020 level of 5.7%), and gradually recover to 6.3% / 6.3% in 2023-24E supported by improving costs control, and better product mix (more exposure from CSP, components, and automotive). With a lower GM, our EPS estimates are down by 5% / 1% for 2022 / 23E.

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**Exhibit 1: Earnings revisions**

NT m	2022E			2023E		
	Old	New	Chg	Old	New	Chg
Revenues	5,735,305	6,008,778	5%	5,723,997	5,781,336	1%
GP	365,935	359,428	-2%	373,592	362,148	-3%
OP	156,733	148,658	-5%	170,464	163,984	-4%
Net income	145,587	139,493	-4%	147,250	147,127	0%
EPS	10.35	9.84	-5%	10.46	10.38	-1%
<b>Margins</b>						
GM	6.4%	6.0%		6.5%	6.3%	
OPM	2.7%	2.5%		3.0%	2.8%	
NM	2.5%	2.3%		2.6%	2.5%	

The EPS is diluted EPS

Source: Goldman Sachs Global Investment Research

**Valuation:** We continue to use PE methodology to derive target price and roll over to 2023 from 2022. With forward year earnings growth largely unchanged at 1% YoY, we keep our target PE multiple unchanged at 11x, which is in line with the company's historical trading average. Our 12-month target price is thus unchanged at NT\$114 (11x 2023E PE). Maintain Neutral.

**Upside risks:** Better-than-expected outlook for iPhone shipments; lower-than-expected opex ratio caused by a further increase in automated production, or further cost control on SG&A.

**Downside risks:** A strong USD against RMB/TWD is a key downside risk given Apple is its main customer, contributing to 40-50% of revenues based on our estimates. Hon Hai's factories are located mainly in mainland China, with costs based in Rmb.

## Exhibit 2: Hon Hai financials summary

Hon Hai (2317.TW)	2019	2020	2021	2022E	2023E	2024E
<b>NTD bn</b>						
<b>P&amp;L</b>						
Revenue	5,343	5,358	5,994	6,009	5,781	5,606
COGS	(5,027)	(5,055)	(5,632)	(5,649)	(5,419)	(5,252)
<b>Gross profit</b>	<b>316</b>	<b>303</b>	<b>362</b>	<b>359</b>	<b>362</b>	<b>354</b>
Operating expense	(201)	(192)	(213)	(211)	(198)	(187)
<b>EBITDA</b>	<b>182</b>	<b>176</b>	<b>224</b>	<b>230</b>	<b>248</b>	<b>253</b>
D&A	(67)	(65)	(75)	(81)	(84)	(86)
<b>EBIT</b>	<b>115</b>	<b>111</b>	<b>149</b>	<b>149</b>	<b>164</b>	<b>167</b>
Net interest income/(expense)	9	8	10	2	2	5
Disposal of assets (pre-tax)	1	(0)	4	0	0	0
Others	39	27	30	27	21	17
<b>Pretax profit</b>	<b>164</b>	<b>145</b>	<b>194</b>	<b>178</b>	<b>187</b>	<b>188</b>
Income tax	(32)	(31)	(40)	(38)	(40)	(41)
Minorities	(17)	(13)	(15)	0	0	0
<b>Net income pre-preferred dividends</b>	<b>115</b>	<b>102</b>	<b>139</b>	<b>139</b>	<b>147</b>	<b>148</b>
Preferred dividends	0	0	0	0	0	0
<b>Net income (pre-exceptionals)</b>	<b>115</b>	<b>102</b>	<b>139</b>	<b>139</b>	<b>147</b>	<b>148</b>
Post-tax exceptionals	0	0	0	0	0	0
<b>Net income</b>	<b>115</b>	<b>102</b>	<b>139</b>	<b>139</b>	<b>147</b>	<b>148</b>
EPS (NTD)	8.2	7.3	9.9	9.8	10.4	10.4
DPS (NTD)	4.2	4.0	4.0	4.0	4.0	4.0
Dividend payout ratio	50%	54%	40%	41%	39%	38%

<b>Growth &amp; margins</b>						
Revenue growth	0.9%	0.3%	11.9%	0.2%	-3.8%	-3.0%
EBITDA growth	-7.2%	-3.3%	27.6%	2.3%	8.2%	1.8%
EBIT growth	-15.6%	-3.5%	34.4%	-0.2%	10.3%	1.6%
Net income growth	-10.7%	-11.7%	36.9%	0.1%	5.5%	0.5%
EPS growth	2.4%	-11.6%	36.4%	-0.7%	5.5%	0.5%
Gross margin	5.9%	5.7%	6.0%	6.0%	6.3%	6.3%
EBITDA margin	3.4%	3.3%	3.7%	3.8%	4.3%	4.5%
EBIT margin	2.2%	2.1%	2.5%	2.5%	2.8%	3.0%

<b>NTD bn</b>						
<b>Quarterly</b>						
	2Q21	3Q21	4Q21	1Q22E	2Q22E	3Q22E
Revenue	1,351.5	1,405.8	1,889.8	1,408.2	1,353.9	1,395.4
EBIT	32.5	36.2	52.7	32.1	25.7	39.4
EBIT margin	2.4%	2.6%	2.8%	2.3%	1.9%	2.8%
Pretax profit	44.2	47.9	62.2	39.3	33.0	46.7
Net income	29.8	37.0	44.4	30.9	25.9	36.7

<b>NTD bn</b>						
<b>Cash flow statement</b>						
	2019	2020	2021	2022E	2023E	2024E
Net income	115	102	139	139	147	148
D&A add-back	67	65	75	81	84	86
Minorities add-back	17	13	15	0	0	0
Net(inc)/dec working capital	93	182	(298)	14	(27)	9
Other operating cash flow	(44)	16	(29)	0	0	0
<b>Cash flow from operations</b>	<b>248</b>	<b>378</b>	<b>(98)</b>	<b>235</b>	<b>204</b>	<b>243</b>
Capital expenditures	(78)	(66)	(92)	(93)	(89)	(86)
(Acquisitions)/divestitures	28	11	(5)	0	0	0
Others	120	89	6	0	0	0
<b>Cash flow from investments</b>	<b>71</b>	<b>35</b>	<b>(92)</b>	<b>(93)</b>	<b>(89)</b>	<b>(86)</b>
Dividend paid (common & pref)	(55)	(58)	(55)	(56)	(57)	(57)
Inc/(dec) in debt	(109)	86	124	0	0	0
Share repurchase/issue (change in common)	0	0	0	0	0	0
Other financing cash flows	(53)	(53)	(44)	0	0	0
<b>Cash flow from financing</b>	<b>(218)</b>	<b>(25)</b>	<b>24</b>	<b>(56)</b>	<b>(57)</b>	<b>(57)</b>
<b>Total cash flow</b>	<b>101</b>	<b>387</b>	<b>(166)</b>	<b>86</b>	<b>58</b>	<b>100</b>
<b>Free cash flow</b>	<b>170</b>	<b>312</b>	<b>(191)</b>	<b>142</b>	<b>115</b>	<b>157</b>

<b>NTD bn</b>						
<b>Balance sheet</b>						
	2019	2020	2021	2022E	2023E	2024E
Cash & equivalent	858	1,233	1,059	1,146	1,204	1,304
Net receivables	1,032	942	1,161	1,144	1,201	1,165
Inventory	516	582	672	659	707	703
Other current asset	2,574	2,885	3,034	3,090	3,253	3,314
<b>Total current assets</b>	<b>2,887</b>	<b>2,877</b>	<b>3,100</b>	<b>3,227</b>	<b>3,336</b>	<b>3,400</b>
Net PP&E	41	47	45	40	36	32
Total investments	337	175	195	195	195	195
Other long-term assets	81	280	324	324	324	324
<b>Total assets</b>	<b>3,321</b>	<b>3,674</b>	<b>3,909</b>	<b>3,976</b>	<b>4,144</b>	<b>4,205</b>
Account payables	906	1,066	1,076	1,060	1,138	1,107
Short-term debt	434	503	585	585	585	585
Other current liabilities	317	347	337	337	337	337
<b>Total current liabilities</b>	<b>1,657</b>	<b>1,916</b>	<b>1,998</b>	<b>1,982</b>	<b>2,060</b>	<b>2,029</b>
Long-term debt	217	233	276	276	276	276
Other long-term liabilities	47	51	62	62	62	62
Total long-term liabilities	264	284	338	338	338	338
<b>Total liabilities</b>	<b>1,921</b>	<b>2,200</b>	<b>2,336</b>	<b>2,320</b>	<b>2,398</b>	<b>2,367</b>
Total common equity	1,240	1,297	1,380	1,463	1,554	1,645
Minority interest	160	177	193	193	193	193
<b>Total equity</b>	<b>1,400</b>	<b>1,474</b>	<b>1,573</b>	<b>1,656</b>	<b>1,746</b>	<b>1,838</b>

Source: Company data, Goldman Sachs Global Investment Research

2317.TW

12m Price Target: NT\$114.00

Price: NT\$102.00

Upside: 11.8%

Neutral

GS Forecast

	12/21	12/22E	12/23E	12/24E
Market cap: NT\$1.4tr / \$48.0bn				
Enterprise value: NT\$1.3tr / \$44.8bn				
3m ADTV: NT\$2.7bn / \$93.8mn				
Taiwan				
Greater China Technology				
M&A Rank: 3				
Leases incl. in net debt & EV?: No				
<b>Revenue (NT\$ mn) New</b>	<b>5,994,173.9</b>	<b>6,008,778.1</b>	<b>5,781,335.9</b>	<b>5,605,847.5</b>
Revenue (NT\$ mn) Old	5,961,967.6	5,735,305.3	5,723,997.2	-
EBITDA (NT\$ mn)	224,440.7	229,559.4	248,396.1	252,802.2
<b>EPS (NT\$) New</b>	<b>9.90</b>	<b>9.84</b>	<b>10.38</b>	<b>10.43</b>
EPS (NT\$) Old	10.14	10.50	10.62	-
P/E (X)	11.3	10.4	9.8	9.8
P/B (X)	1.1	1.0	0.9	0.9
Dividend yield (%)	3.6	3.9	3.9	3.9
CROCI (%)	13.5	13.3	13.2	12.5
EPS (NT\$)	3.13	2.18	1.83	2.59

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 29 Apr 2022 close.

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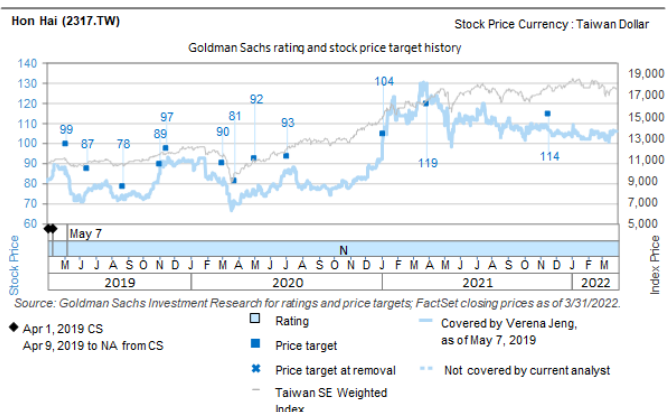
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