

# Xiaomi Corporation

Supply-demand imbalance weighed on results, shift towards user experience to gain differentiated edges, maintain Buy

## Maintain Buy on differentiated move

We maintain Buy on Xiaomi despite the declining results in Q2, which is attributable to: 1) the consumer demand recovery was slower than expected; 2) supply-demand imbalance weighed on margins caused by knock-on effect of supply chain crunch; 3) opex burden from new business. However, we see all of these headwinds are transitory and will be fading away in 2H. In addition, we noticed from its latest new product launch that Xiaomi is strategically shifting focus towards user experience, which is significantly different from Android camp's focus on hardware. We believe it will help Xiaomi to differentiate itself from other players and continue to strengthen its position in certain segments of smart devices sector.

## Smartphone: shifting towards user experience to gain differentiated edges

According to Canalys, Xiaomi's total global shipments was 39.1mn units in Q2, down 25% YoY but up 1.5% QoQ, maintaining the 3<sup>rd</sup> place in market share of 13.8%. Smartphone revenue declined by 28.5% YoY to RMB42.3bn, mainly due to the slower-than-expected demand recovery and few new product launches in Q2. Gross margin down 1.2ppts from 9.9% in Q1 to 8.7% in Q2, due to increased inventory and supply-demand imbalance caused by knock-on effect of supply chain crunch. However, with rising consumer sentiment and new high-end launches, such as Mi13, in 2H, we expect Xiaomi's smartphone shipment will be back on growth trajectory. On the other hand, we noticed that Xiaomi is strategically shifting focus towards user experience. For its latest MIX Fold 2, Xiaomi almost redefined the usage scenario of foldable smartphone, in contrast to hardware spec focus competition within the Android camp, which will further strengthen Xiaomi's position in the premium market, in our view.

## AIoT & internet: made steady progress in big white appliance

AIoT revenue was RMB19.8bn in Q2, down 4.5% YoY/ up 1.7% QoQ. Smart TV global shipments grew to 2.6mn units in Q2, outperforming global TV market and maintaining the leadership in mainland China and top 5 globally. Meanwhile, Xiaomi made steady progress in big white appliances, such as smart AC, refrigerator, and washing machine, of which shipment increased substantially in Q2. In addition, No. of AIoT platform devices exceeded 526.9mn units globally as of Q2, up 40.7% YoY, in particular, No. of users with five or more smart devices connected reached 10.2mn. We believe the user's stickiness and improving ecosystem will drive AIoT growth in the future. In Q2, internet services revenue was down by 0.9% YoY to RMB7.0bn with a gross margin of 73.0%. Despite a declining smartphone shipment, global MIUI MAU increased to 547mn.

## Q2 results recap & valuation adjustment

In Q2, Xiaomi's total revenue was RMB70.2bn, down 20.1% YoY. Gross margin was 16.8% vs 17.3% in Q1. Opex ratio rose sequentially to 14.8% in Q2 from 13.6% last quarter because of new business/EV investment ramping. Adj. net profit came in at RMB2.1bn, down 67.1% YoY. Considering the slower-than-expected demand recovery, we revised down Xiaomi's FY22e smartphone shipment forecast to 161mn units and our FY22e/FY23e EPS forecasts to RMB0.49/shr/RMB0.65/shr. Nevertheless, our LT view on Xiaomi is intact and we maintain Buy on Xiaomi with a lower PT of HK\$17.0 on 23x FY23e P/E.

## Risks

Key risks to our PT include: 1) prolonged COVID-19 pandemic; 2) worse-than-expected chip supply constraints; 3) more-than-expected EV upfront investment.

Stock code: 1810.HK

Rating: Buy

<b>Price target (HK\$)</b>	<b>17.0</b>
Current price (HK\$, 22 August 2022)	11.3
Upside/downside %	51%
Market cap (HK\$ m)	281,519
Market cap (US\$ m)	35,882
Avg daily turnover (HK\$ m)	1,574

Source: Bloomberg, AMTD Research

## Key forecasts

(Rmb m)	2021	2022e	2023e
Non-IFRS net profit	22,040	12,740	16,721
yoy %	69%	-42%	31%
Revenue	328,309	305,368	361,206
yoy %	34%	-7%	18%
Smartphone shipment (mn units)	190	161	194
yoy %	30%	-15%	20%
Gross margin	17.7%	17.0%	17.2%
Non-IFRS net margin	6.7%	4.2%	4.6%
EPS (RMB/sh)	0.86	0.49	0.65

Source: Company data, AMTD Research estimates

## Valuation

	2021	2022e	2023e
P/E (adjusted)	10.6	18.5	14.1
P/S	0.7	0.7	0.6
ROE	16.4%	8.4%	10.0%
ROA	8.4%	4.6%	5.4%

Source: Bloomberg, AMTD Research estimates

## Share price performance



Source: Bloomberg

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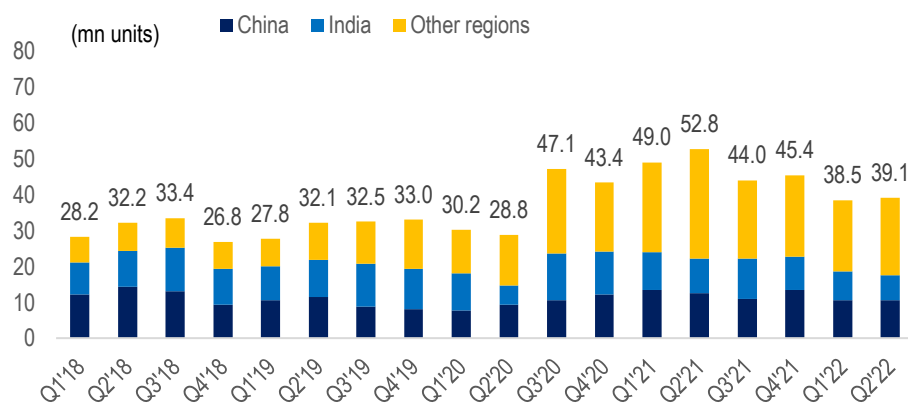
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## Smartphone shipment

Figure 1: Xiaomi's quarterly smartphone shipment, by region



Source: Canalys, AMTD Research

## Valuation

Figure 2: One year forward P/E of Xiaomi



Source: Bloomberg, AMTD Research estimates

Figure 3: Xiaomi's quarterly P&amp;L

Rmb m	2Q20	3Q20	4Q20	1Q21	2Q21	3Q21	4Q21	1Q22	2Q22
<b>Profit &amp; loss</b>									
<b>Revenue</b>	<b>53,538</b>	<b>72,163</b>	<b>70,462</b>	<b>76,882</b>	<b>87,789</b>	<b>78,063</b>	<b>85,575</b>	<b>73,352</b>	<b>70,171</b>
Smartphones	31,628	47,604	42,634	51,491	59,089	47,825	50,464	45,763	42,268
IoT and lifestyle products	15,253	18,119	21,054	18,243	20,735	20,936	25,067	19,477	19,812
Internet services	5,908	5,772	6,175	6,571	7,034	7,338	7,270	7,113	6,971
Others	750	668	599	577	932	1,965	2,775	999	1,120
<b>Cost of sales</b>	<b>(45,836)</b>	<b>(61,997)</b>	<b>(59,137)</b>	<b>(62,721)</b>	<b>(72,641)</b>	<b>(63,771)</b>	<b>(70,916)</b>	<b>(60,642)</b>	<b>(58,403)</b>
<b>Gross profit</b>	<b>7,701</b>	<b>10,166</b>	<b>11,325</b>	<b>14,161</b>	<b>15,148</b>	<b>14,292</b>	<b>14,660</b>	<b>12,710</b>	<b>11,768</b>
<b>Gross margin</b>	<b>14.4%</b>	<b>14.1%</b>	<b>16.1%</b>	<b>18.4%</b>	<b>17.3%</b>	<b>18.3%</b>	<b>17.1%</b>	<b>17.3%</b>	<b>16.8%</b>
<b>Operating expenses</b>	<b>(6,018)</b>	<b>(6,775)</b>	<b>(9,472)</b>	<b>(8,163)</b>	<b>(9,895)</b>	<b>(9,395)</b>	<b>(11,434)</b>	<b>(9,995)</b>	<b>(10,411)</b>
Selling and marketing expenses	(3,224)	(3,601)	(5,090)	(4,164)	(5,681)	(4,882)	(6,254)	(5,256)	(5,332)
Administrative expenses	(836)	(853)	(1,276)	(988)	(1,150)	(1,275)	(1,326)	(1,245)	(1,315)
R&D expenses	(1,958)	(2,321)	(3,106)	(3,012)	(3,064)	(3,238)	(3,853)	(3,495)	(3,763)
<b>EBIT</b>	<b>1,683</b>	<b>3,391</b>	<b>1,854</b>	<b>5,998</b>	<b>5,253</b>	<b>4,898</b>	<b>3,226</b>	<b>2,714</b>	<b>1,357</b>
Fair value changes on investments	2,366	3,418	7,042	2,063	4,165	(1,976)	3,879	(3,550)	514
Share of losses of investments	893	(11)	368	9	(26)	45	247	(201)	63
Other income	183	139	247	152	235	235	205	165	186
Other (losses)/gains, net	288	(241)	91	(65)	1,099	(472)	(3,142)	(39)	(386)
<b>PBT</b>	<b>4,868</b>	<b>5,451</b>	<b>8,861</b>	<b>9,067</b>	<b>9,679</b>	<b>1,787</b>	<b>3,885</b>	<b>(416)</b>	<b>1,737</b>
Income tax expenses	(374)	(586)	(66)	(1,278)	(1,415)	(999)	(1,442)	(115)	(372)
<b>(Loss)/profit for the year</b>	<b>4,493</b>	<b>4,864</b>	<b>8,795</b>	<b>7,789</b>	<b>8,263</b>	<b>789</b>	<b>2,443</b>	<b>(531)</b>	<b>1,365</b>
Minority interest	(5)	(16)	(18)	(4)	(4)	4	(51)	57	(21)
<b>Attributable profit</b>	<b>4,498</b>	<b>4,881</b>	<b>8,813</b>	<b>7,793</b>	<b>8,268</b>	<b>785</b>	<b>2,494</b>	<b>(588)</b>	<b>1,386</b>
<b>Adjusted net profit (non-IFRS)</b>	<b>3,373</b>	<b>4,128</b>	<b>3,204</b>	<b>6,069</b>	<b>6,322</b>	<b>5,176</b>	<b>4,473</b>	<b>2,859</b>	<b>2,081</b>
<b>YoY growth %</b>									
<b>Total revenue</b>	<b>3%</b>	<b>34%</b>	<b>25%</b>	<b>55%</b>	<b>64%</b>	<b>8%</b>	<b>21%</b>	<b>-5%</b>	<b>-20%</b>
Smartphones	-1%	48%	38%	70%	87%	0%	18%	-11%	-28%
IoT and lifestyle products	2%	16%	8%	41%	36%	16%	19%	7%	-4%
Internet services	29%	9%	8%	11%	19%	27%	18%	8%	-1%
Others	85%	40%	24%	17%	24%	194%	364%	73%	20%
<b>Gross profit</b>	<b>6%</b>	<b>23%</b>	<b>44%</b>	<b>87%</b>	<b>97%</b>	<b>41%</b>	<b>29%</b>	<b>-10%</b>	<b>-22%</b>
<b>Adjusted net profit (non-IFRS)</b>	<b>-7%</b>	<b>19%</b>	<b>37%</b>	<b>164%</b>	<b>87%</b>	<b>25%</b>	<b>40%</b>	<b>-53%</b>	<b>-67%</b>

Source: Company data; AMTD research

Figure 4: Xiaomi's P&amp;L forecast

Rmb m	2018	2019	2020	2021	2022E	2023E
<b>Profit &amp; loss</b>						
<b>Revenue</b>	<b>174,915</b>	<b>205,839</b>	<b>245,866</b>	<b>328,309</b>	<b>305,368</b>	<b>361,206</b>
Smartphones	113,800	122,095	152,190	208,869	184,445	225,045
IoT and lifestyle products	43,817	62,088	67,411	84,980	83,746	94,061
Internet services	15,956	19,842	23,755	28,212	30,616	35,211
Others	1,343	1,814	2,509	6,248	6,561	6,889
<b>Cost of sales</b>	<b>(152,723)</b>	<b>(177,285)</b>	<b>(209,114)</b>	<b>(270,048)</b>	<b>(253,398)</b>	<b>(299,249)</b>
<b>Gross profit</b>	<b>22,192</b>	<b>28,554</b>	<b>36,752</b>	<b>58,261</b>	<b>51,970</b>	<b>61,957</b>
<b>Gross margin</b>	<b>12.7%</b>	<b>13.9%</b>	<b>14.9%</b>	<b>17.7%</b>	<b>17.0%</b>	<b>17.2%</b>
<b>Operating expenses</b>	<b>(25,869)</b>	<b>(20,975)</b>	<b>(27,542)</b>	<b>(38,887)</b>	<b>(40,003)</b>	<b>(44,067)</b>
Selling and marketing expenses	(7,993)	(10,378)	(14,539)	(20,981)	(20,765)	(22,756)
Administrative expenses	(12,099)	(3,104)	(3,746)	(4,739)	(4,886)	(5,057)
R&D expenses	(5,777)	(7,493)	(9,256)	(13,167)	(14,352)	(16,254)
<b>EBIT</b>	<b>(3,677)</b>	<b>7,580</b>	<b>9,210</b>	<b>19,374</b>	<b>11,967</b>	<b>17,890</b>
<b>PBT</b>	<b>13,927</b>	<b>12,163</b>	<b>21,633</b>	<b>24,417</b>	<b>14,267</b>	<b>18,690</b>
Income tax expenses	(449)	(2,060)	(1,321)	(5,134)	(1,527)	(1,969)
<b>(Loss)/profit for the year</b>	<b>13,478</b>	<b>10,103</b>	<b>20,313</b>	<b>19,283</b>	<b>12,740</b>	<b>16,721</b>
Minority interest	(76)	59	(43)	(56)	(62)	(68)
<b>Attributable profit</b>	<b>13,554</b>	<b>10,044</b>	<b>20,356</b>	<b>19,339</b>	<b>12,802</b>	<b>16,789</b>
<b>Adjusted net profit (non-IFRS)</b>	<b>8,555</b>	<b>11,532</b>	<b>13,006</b>	<b>22,040</b>	<b>12,740</b>	<b>16,721</b>
<b>Yoy growth %</b>						
<b>Total revenue</b>	<b>53%</b>	<b>18%</b>	<b>19%</b>	<b>34%</b>	<b>-7%</b>	<b>18%</b>
Smartphones	41%	7%	25%	37%	-12%	22%
IoT and lifestyle products	87%	42%	9%	26%	-1%	12%
Internet services	61%	24%	20%	19%	9%	15%
Others	87%	35%	38%	149%	5%	5%
<b>Gross profit</b>	<b>46%</b>	<b>29%</b>	<b>29%</b>	<b>59%</b>	<b>-11%</b>	<b>19%</b>
<b>(Loss)/profit for the year (reported)</b>	<b>na</b>	<b>-25%</b>	<b>101%</b>	<b>-5%</b>	<b>-34%</b>	<b>31%</b>
<b>Adjusted net profit (non-IFRS)</b>	<b>60%</b>	<b>35%</b>	<b>13%</b>	<b>69%</b>	<b>-42%</b>	<b>31%</b>

Source: Company data; AMTD Research estimates

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<b>Buy</b>	Stock with potential return of over 20% over the next 12 months
<b>Hold</b>	Stock with potential return of -20% to +20% over the next 12 months
<b>Sell</b>	Stock with potential loss of over 20% over the next 12 months

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