



July 16, 2015
Company Report
Rating: BUY
TP: HK\$5.0

H-Share price (HK\$) 3.38
Est. share price return 47.93%
Est. dividend yield 0.00%
Est. total return 47.93%

Previous Rating & TP BUY, HK\$3.27
Previous Report Date Jan. 28, 2015

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Key Data

52Wk H/L(HK\$) 5.79/2.12
Issued shares (mn) 2,039
Market cap (HK\$ mn) 6,892
3-mth avg daily turnover (HK\$ mn) 217.6
Major shareholder(s) (%):
Chen Yuhong 12.48

Source(s): Company, Bloomberg, ABCI Securities

FY14 revenue breakdown (%)

Software & hardware products 6.37
Professional services 38.47
Outsourcing services 45.75
Training 2.06
Emerging services business 7.36
Sum 100.00

Source(s): Company, ABCI Securities

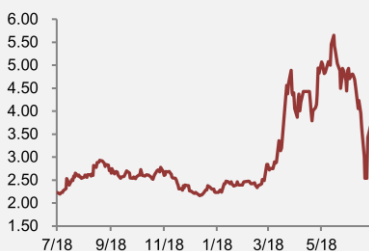
Share performance (%)

	Absolute	Relative*
1-mth	(23.87)	(18.19)
3-mth	(23.18)	(13.51)
6-mth	51.57	47.62

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

1-Year stock performance (HK\$)



Source(s): Bloomberg, ABCI Securities

ChinaSoft Int'l (354 HK)

Site visit: smooth development of JointForce

- JointForce (JF), CSI's crowdsourcing platform, was officially launched on June 19. Since then, JF has attracted ~1300 clients from both IT and non-IT sectors and over 200 service groups with ~39,000 software developers.
- JF will boost CSI's profitability by reducing costs and creating a new business model. However, it would take time before JF can evolve into a successful platform. Based on its FY14 results, our FY15E NP / EPS are RMB 276.59mn/0.146, up 38.27%/38.24%YoY
- We believe JF will benefit from China's Internet Plus strategy and popularity of mobile internet in China. Its current valuation is attractive at 0.5x/0.3x FY15E/16E PEG and we reiterate BUY with a 12-mth TP of HK\$ 5.0, reflecting 0.5x FY16E PEG.

Here are the key takeaways from our discussion with the management of ChinaSoft Int'l in Beijing after our visit in July 2015:

JF highly welcomed by both small and large firms. JF is a crowdsourcing platform officially launched for business use on June 19, 2015. It connects software developers (bidders) and companies with IT needs (contract issuers). For small and medium (S&M) issuers (1~200 staffs), JF can provide bidders who provide product design including websites, mobile apps, and IT system maintenance services at low prices; for large issuers, CSI can help them outsource contracts to highly qualified IT developers.

Benefits of using JF include: 1) More efficient communication between IT service providers and end-users, as JF staffs can help translate end-users' requests to the service providers more efficiently with terms the IT professionals are familiar with ; 2) Significantly reduce HR costs and agency problems between in-house IT staffs and the management. 3) Firms are more likely to find the most suitable programmers that fulfill the job requirements. CSI also plans to connect its JF platform with WeChat's enterprises public accounts. We believe the mobile internet will boost the use of JF.

Registered users are growing quickly. 1) Since June 19, JF had 1300 registered issuers. CSI expected the number to continue to rise in light of the huge demand triggered by China's Internet Plus and Industry 4.0 initiatives; 2) 400 engineer groups have logged onto JF; 200 groups with over 39,000 individual programmers nationwide have officially registered. CSI believes the number will keep growing with JF's rising popularity.

A new business model has been established. CSI is benefiting from JF in the following ways: 1) CSI will charge 10% of the contract amount from the bidders as servicing fees; 2) Potential interest benefit from deposits from issuers. 3) By using JF, CSI can distribute its own contracts. Internal tests showed that the net profit margin of business contracts from the government sector can be elevated by 9ppt by outsourcing; 4) CSI will provide advertising and IT headhunting services through JF.

Results and Valuation

FY ended Dec 31	2012A	2013A	2014A	2015E	2016E
Turnover (RMB '000)	2,768,171	3,205,985	4,429,202	5,589,922	7,155,197
Chg (%.yoy)	23.37	15.82	38.15	26.21	28.00
Net Income (RMB '000)	133,189	148,301	200,038	276,592	384,909
Chg (%.YoY)	20.43	11.35	34.89	38.27	39.16
EPS (RMB)	0.077	0.082	0.105	0.146	0.203
Chg (%.YoY)	2.38	6.46	27.91	38.24	39.16
BVPS (RMB)	1.12	1.26	1.32	1.48	1.70
Chg (%.yoy)	-5.05	12.59	4.34	12.37	14.87
DPS,RMB	-	-	-	-	-
P/E (x)	-	-	25.62	18.54	13.32
P/B (x)	-	-	2.05	1.83	1.59
Yield (%)	-	-	-	-	-
ROE (%)	7.29	7.07	8.40	10.43	12.77
ROA (%)	3.87	3.17	3.74	4.59	5.27

Source(s): Bloomberg, ABCI Securities estimates

JF's contribution will be limited in the short term. While JF has a relatively smooth start, we do not expect the platform to contribute significantly to revenue in the short term because 1) it would take time to finesse the procedure arrangement in JF; 2) more effort will be needed to promote the JF platform; 3) CSI will need more experiences in tackling potential risks such as protecting itself from potential intelligence property (IP) disputes between issuers and bidders. Though IP protection is not a major concern for most Chinese S&M issuers at present, we believe potential conflicts would arise when more issuers become aware of the value of IP.

Maintain BUY on attractive valuation. We believe the JF platform would improve the Group's GPM and NPM gradually. We estimate the Group's NPM to be 6.31% in FY15E, only slightly higher than its FY14 NPM of 5.76%. Our FY15E GPM is 31.5%. Based on its FY14 results, our FY15E NP / EPS are RMB 276.59mn/0.146, up 38.27%/38.24%YoY. The Group is trading at 0.5x/0.3x FY15E/16E PEG and we believe the positives, including the potential contribution from JF, have not been fully accounted for. The counter's current valuation is still attractive and we reiterate **BUY** with TP at HK\$5.0, reflecting 0.5x FY16E PEG.

Risk factors: 1) Slower-than-expected development in cloud service and big data business; 2) Failure of JF to attract IT talents and clients; 3) Intensifying competition with domestic peers; (4) Post-merger risks with Catapult; (5) No dividends payment expected in FY15E/16E.



Consolidated income statement (2012A-2016E)

FY Ended Dec 31 (RMB '000)	2012A	2013A	2014A	2015E	2016E
Sale of software and hardware products	216,776	138,058	282,187	310,406	341,446
Professional services	1,236,006	1,430,498	1,703,703	2,027,407	2,432,888
Outsourcing services	1,221,800	1,388,388	2,026,301	2,735,506	3,692,934
Training	93,589	94,363	91,114	92,936	94,795
Emerging services business	0	154,678	325,898	423,667	593,134
Revenues	2,768,171	3,205,985	4,429,203	5,589,922	7,155,197
Cost of revenues	(1,852,830)	(2,200,799)	(3,080,046)	(3,829,097)	(4,901,310)
Gross profit	915,341	1,005,186	1,349,157	1,760,826	2,253,887
SG&A	(615,453)	(687,592)	(884,541)	(1,105,955)	(1,395,765)
Other income and gains	112,172	112,676	167,377	239,971	280,742
Pre-tax profit	187,716	204,918	297,239	414,900	577,381
Income tax	(37,574)	(4,890)	(42,183)	(62,235)	(86,607)
Net profit	150,142	200,028	255,056	352,665	490,774
Profit attributable to:					
Minority interests	16,953	51,727	55,018	76,073	105,865
Equity holders of the Company	133,189	148,301	200,038	276,592	384,909
EPS (Basic), RMB	0.080	0.084	0.107	0.148	0.206
EPS, Diluted, RMB	0.077	0.082	0.105	0.146	0.203
DPS, RMB	-	-	-	-	-

Source(s): Company, ABCI Securities estimates

Consolidated balance sheet (2012A-2016E)

As of Dec 31 (RMB'000)	2012A	2013A	2014A	2015E	2016E
PP&E	132,853	174,186	335,803	254,995	295,399
Intangible assets	159,330	280,649	325,458	303,054	314,256
Interests in associates	27,616	13,519	9,629	9,259	7,555
Other non-current assets	707,067	1,029,358	1,079,621	514,094	759,745
Total non-current assets	1,026,866	1,497,712	1,750,511	1,081,402	1,376,954
Inventories	23,989	19,883	31,991	27,950	35,776
Accounts receivable	1,039,396	1,146,646	1,315,781	1,956,473	2,504,319
Prepayments, deposits and other assets	1,038	1,009	1,009	1,009	1,009
Cash and cash equivalents	774,847	940,823	811,435	1,101,591	1,001,964
Other current assets	576,214	1,066,884	1,433,739	1,859,339	2,380,204
Current Assets	2,415,484	3,175,245	3,593,955	4,946,362	5,923,272
Total assets	3,442,350	4,672,957	5,344,466	6,027,763	7,300,226
Amounts due to customers for contract work	110,506	217,410	212,205	323,445	378,412
Trade and other payables	668,918	741,528	771,852	1,133,522	1,348,912
Bills payable	7,071	3,387	35,791	2,795	3,578
Taxation payable	39,312	28,303	52,651	40,477	46,564
Borrowings	309,300	471,328	1,240,190	855,759	1,047,975
Other short-term liabilities	208,358	9,269	16,781	18,633	25,447
Total current liabilities	1,343,465	1,471,225	2,329,470	2,374,631	2,850,887
Deferred tax liabilities	17,602	17,589	19,294	18,442	18,868
Borrowings	19,000	518,268	62,000	290,134	176,067
Other Non-current Liabilities	0	224,674	232,671	228,673	230,672
Total non-current liabilities	36,602	760,531	313,965	537,248	425,607
Total liabilities	1,380,067	2,231,756	2,643,435	2,911,879	3,276,494
Total equity	2,062,283	2,441,201	2,701,031	3,115,884	4,023,733
Non-controlling interests	134,659	172,978	203,652	309,565	800,023
Equity of the firm	1,927,624	2,268,223	2,497,379	2,806,319	3,223,709
BVPS, Diluted	1.12	1.26	1.32	1.48	1.70

Source(s): Company, ABCI Securities estimates



Consolidated cash flow statement (2012A-2016E)

FY ended Dec 31 (RMB'000)	2012A	2013A	2014A	2015E	2016E
Profit before taxation	187,716	204,918	297,239	414,900	577,381
Adjustments for:					
Depreciation of property, plant and equipment	46,577	52,562	60,137	73,254	86,704
Amortization of intangible assets and prepaid lease payments	42,967	49,803	80,676	65,240	72,958
Finance costs	31,111	47,296	84,385	47,296	47,296
Interest income	(3,326)	(1,958)	(2,847)	(2,403)	(2,625)
Loss on disposal of property, plant and equipment	137	1,114	193	654	423
Impairment loss recognized in respect of goodwill	28,054	0	0	0	0
Other adjusted items	19,764	30,629	14,248	50,807	62,535
Operating cash flows before movements in working capital	353,000	384,364	534,031	649,747	844,673
Working Capital Changes					
Increase in trade and other receivables	(294,161)	(78,908)	(117,756)	(320,346)	(273,923)
Increase in amounts due to customers for contract work	54,364	106,904	(5,205)	111,240	54,967
Increase in amounts due from customers for contract work	(197,676)	(490,881)	(349,556)	(434,249)	(516,541)
Increase in trade and other payables	55,769	36,886	18,674	361,670	215,390
Decrease in inventories	416	4,106	(12,108)	4,041	(7,826)
Decrease in bills payable	(14,454)	(3,684)	32,404	(32,996)	783
Cash used in operations	(42,742)	(41,213)	100,484	339,107	317,522
Other adjusted items	(35,624)	(19,825)	(25,688)	(22,757)	(24,222)
Net cash generated from operating activities	(78,366)	(61,038)	74,796	316,351	293,300
Investing activities					
Acquisition of a subsidiary	0	(226,887)	0	(113,444)	(56,722)
Purchases of property, plant and equipment	(50,145)	(80,663)	(215,076)	(147,870)	(181,473)
Development costs paid	(41,619)	(59,689)	(79,436)	(69,563)	(74,499)
Purchase of software	(3,351)	(17,356)	(5,785)	(11,571)	(8,678)
Proceeds from disposal of property, plant and equipment	1,950	2,466	5,653	4,060	4,856
Interest received	3,326	1,958	2,847	2,403	2,625
Other adjusted items	(39,483)	(82,557)	(146,375)	(96,374)	(103,282)
Net cash used in investing activities	(129,322)	(462,728)	(438,172)	(432,358)	(417,172)
Cash flows from financing activities					
New bank loans raised	284,300	1,059,558	1,273,787	1,033,148	769,172
Repayment of borrowings	(151,200)	(413,504)	(961,193)	(687,349)	(824,271)
Other adjusted items	77,054	(361,988)	(76,796)	65,183	82,658
Net cash flows (used in)/generated from financing activities	210,154	697,570	235,798	410,982	27,560
Net increase in cash and cash equivalents	2,466	173,804	(127,578)	294,975	(96,313)
Cash and cash equivalents at beginning of the year	772,950	774,847	940,823	811,435	1,101,591
Exchange losses on cash and cash equivalents	(569)	(7,828)	(1,810)	(4,819)	(3,315)
Cash and cash equivalents at end of the year	774,847	940,823	811,435	1,101,591	1,001,964

Source(s): Company, ABCI Securities estimates

Financial ratio table (2012A-2016E)

FY Ended Dec 31	2012A	2013A	2014A	2015E	2016E
Gross margin, %	33.07	31.35	30.46	31.50	31.50
Operating margin, %	6.78	6.39	6.71	7.42	8.07
Net margin, %	5.42	6.24	5.76	6.31	6.86
ROE, %	7.29	7.07	8.40	10.43	12.77
ROA, %	3.87	3.17	3.74	4.59	5.27
Total Liability/Total Equity,%	66.92	91.42	97.87	93.45	81.43

Source(s): Company, ABCI Securities estimates

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Definition of equity rating

Rating	Definition
Buy	Stock return \geq Market return rate
Hold	Market return $- 6\% \leq$ Stock return $<$ Market return rate
Sell	Stock return $<$ Market return $- 6\%$

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate from 2010-2014

Time horizon of share price target: 12-month

Definition of share price risk

Rating	Definition
Very high	$2.6 \leq$ 180 day volatility/180 day benchmark index volatility
High	$1.5 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 2.6
Medium	$1.0 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 1.5
Low	180 day volatility/180 day benchmark index volatility $<$ 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index.

Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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