



## Company Report: Techtronic Industries (00669 HK)

公司报告: 创科实业 (00669 HK)

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12 November 2020

# Cordless Power Tool Leader Driven by Technological Innovations, Initiate With "Accumulate"

技术创新驱动的充电式电动工具领导者，首予“收集”

- **TTI is a global leader of power tools with focus on the North American market.** We believe that North America will continue to lead the global power tool market in the incoming five years despite great potential in emerging markets. We expect that TTI will continue to win more market share on its well-positioned branding and strategic focus on cordless technology.
- **TTI's product competitiveness has been strengthened by consistently increasing R&D expenditure and rapidly expanding product family.** We believe that TTI will maintain R&D expense ratio above 3%, to significantly outpace its peers. The Home Depot remains as TTI's most powerful distribution channel despite impact from online retailers and the COVID-19 pandemic. In terms of TTI's floor care, we believe a strategic shift towards cordless and carpet washing products will continue to drive its turnaround.
- **We expect TTI's top line and bottom line to grow at a CAGR of 12.5% and 14.7%, respectively, during 2019-2022.** We believe that robust sales of power equipment will continue to drive TTI's revenue growth, while floor care will further recover after the strategic shift. Based on an excellent proven record in the past decade plus bright outlook for ongoing product upgrades, we are confident in TTI's sustainable profit margin improvement.
- **Initiate with "Accumulate" and a TP of HK\$119.30.** We believe that TTI's valuation premium over other major peers could be justified by its higher certainty in consistent improvement in market share and profit margin, despite some short-term pressure on the valuation due to potential reduction of DIY demand once the COVID-19 pandemic is controlled by vaccines. Our TP represents 39.1x/ 34.3x/ 30.2x 2020-2022 PE ratio and 7.3x 2020 PB ratio.
- **创科实业是一家以北美市场为核心的全球电动工具领导者。**尽管新兴市场潜力巨大，我们认为北美将在未来5年内继续引领全球电动工具市场。我们预计凭借其良好的品牌定位以及在充电式技术上的战略聚焦，创科实业将继续赢得更多市场份额。
- **创科实业的产品竞争力因持续增加的研发投入和快速扩张的产品系列而得到增强。**我们认为创科实业的研发费用率将维持在3%以上，显著高于同业。尽管受到电商和新冠疫情的影响，家得宝仍然是创科实业最为强大的分销渠道。就创科实业的地板护理业务而言，我们认为向充电式和地毯清洗产品的战略转移将继续带动其好转。
- **我们预计创科实业 2019-2022 年收入和股东净利将分别以 12.5%和 14.7%的年复合增长率增长。**我们认为，动力设备的强劲销售将继续推动创科实业的收入增长，而地板护理在战略转型后将进一步复苏。基于过去十年来优秀的业绩表现以及产品持续升级换代的光明前景，我们对创科实业利润率的持续改善充满信心。
- **首予“收集”，目标价为 119.30 港元。**我们认为创科实业相对其他主要同业的估值溢价，在其市占率和利润率持续提升的较高确定性下是合理的，尽管一旦新冠疫情被疫苗控制后 DIY 需求可能下滑，估值短期内有一定压力。我们的目标价对应 39.1 倍/ 34.3 倍/ 30.2 倍的 2020-2022 年市盈率及 7.3 倍的 2020 年市净率。

Rating:

**Accumulate**

Initial

评级:

收集 (首次覆盖)

6-18m TP 目标价:

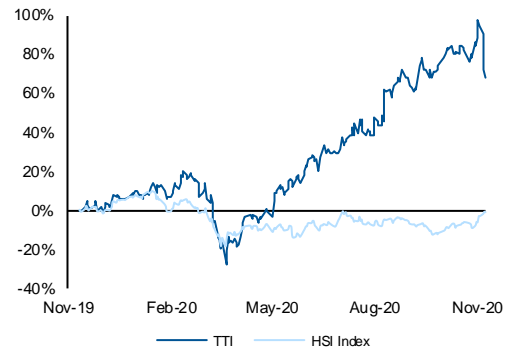
**HK\$119.30**

Share price 股价:

HK\$97.450

### Stock performance

股价表现



Change in Share Price	1 M	3 M	1 Y
股价变动	1 个月	3 个月	1 年
Abs. % 绝对变动 %	(6.8)	17.2	64.4
Rel. % to HS Index 相对恒指变动 %	(13.2)	13.4	67.6
Avg. Share price(HK\$) 平均股价 (港元)	105.6	98.6	73.1

Source: Bloomberg, Guotai Junan International.

Year End	Turnover	Net Profit	EPS	EPS	PER	BPS	PBR	DPS	Yield	ROE
年结	收入	股东净利	每股净利	每股净利变动	市盈率	每股净资产	市净率	每股股息	股息率	净资产收益率
12/31	(US\$ m)	(US\$ m)	(US\$)	(Δ %)	(x)	(US\$)	(x)	(US\$)	(%)	(%)
2018A	7,021	552	0.302	17.5	41.2	1.672	7.4	0.113	0.9	19.1
2019A	7,667	615	0.337	11.6	37.1	1.855	6.7	0.133	1.1	19.1
2020F	8,743	716	0.391	16.0	32.2	2.100	6.0	0.162	1.3	19.8
2021F	9,809	817	0.446	14.1	28.2	2.373	5.3	0.193	1.5	19.9
2022F	10,927	929	0.506	13.5	24.8	2.672	4.7	0.228	1.8	20.1

Shares in issue (m) 总股数 (m)	1,832.3	Major shareholder 大股东	Horst Julius Pudwill 20.0%
Market cap. (HK\$ m) 市值 (HK\$ m)	178,557.6	Free float (%) 自由流通比率 (%)	61.7
3 month average vol. 3 个月平均成交股数 ('000)	3,360.9	FY20 Net gearing (%) FY20 净负债/股东资金 (%)	Net cash
52 Weeks high/low (HK\$) 52 周高/低 (HK\$)	115.000 / 42.100	FY20 Est. NAV (HK\$) FY20 每股估值 (港元)	119.3

Source: the Company, Guotai Junan International.







































See the last page for disclaimer

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**COMPANY PROFILE**

TTI is a global leader of power tools with focus on the North American market. Techtronic Industries (TTI, or the "Company") is a leading manufacturer of power tools, outdoor garden equipment, and floor care equipment. Founded in 1985 and listed on the Hong Kong Stock Exchange in 1990, the Company was a contract manufacturer producing power tools for famous brands such as Craftsman and Ryobi at its early stages. After years of successful transformation from the OEM/ODM model to the OBM model, the Company's brand portfolio has been strongly strengthened through acquisition and licensing. Currently, TTI's brand portfolio includes MILWAUKEE, AEG and RYOBI power tools, accessories and hand tools; RYOBI and HOMELITE outdoor power equipment; EMPIRE layout and measuring products; and HOOVER, ORECK, VAX and DIRT DEVIL floor care and appliances.

**Figure-1: TTI's Brands and Representative Products**

Core Brands	Positioning	Representative Products							
 <b>MILWAUKEE</b> (2005 <sup>^</sup> )	<ul style="list-style-type: none"> <li>Industrial and professional power tools</li> <li>Hand tools and storage</li> </ul>								
 <b>RYOBI*</b> (2000-2004 <sup>^</sup> )	<ul style="list-style-type: none"> <li>Consumer / DIY power tools</li> <li>Outdoor garden equipment</li> </ul>								
 <b>HOOVER</b> (2007 <sup>^</sup> )	<ul style="list-style-type: none"> <li>Premium / commercial floor care</li> </ul>								
Other Brands									
 <b>AEG*</b> (2005 <sup>^</sup> )	 <b>HOMELITE</b> (2002 <sup>^</sup> )	 <b>STILETTO</b> (2007 <sup>^</sup> )	 <b>HART</b>	 <b>IMPERIAL BLADES</b> (2018 <sup>^</sup> )	 <b>EMPIRE</b> (2014 <sup>^</sup> )	 <b>VAX</b> (1999 <sup>^</sup> )	 <b>DIRT DEVIL</b> (2003 <sup>^</sup> )	 <b>ORECK</b> (2013 <sup>^</sup> )	
									
<ul style="list-style-type: none"> <li>Professional power tools</li> </ul>	<ul style="list-style-type: none"> <li>Consumer outdoor garden equipment</li> </ul>	<ul style="list-style-type: none"> <li>Premium lightweight hand tools</li> </ul>	<ul style="list-style-type: none"> <li>Consumer hand tools</li> </ul>	<ul style="list-style-type: none"> <li>Oscillating multi-tool accessories</li> </ul>	<ul style="list-style-type: none"> <li>Layout and measuring tools</li> </ul>	<ul style="list-style-type: none"> <li>High performance floor care</li> </ul>	<ul style="list-style-type: none"> <li>Consumer floor care</li> </ul>	<ul style="list-style-type: none"> <li>Professional / commercial floor care</li> </ul>	

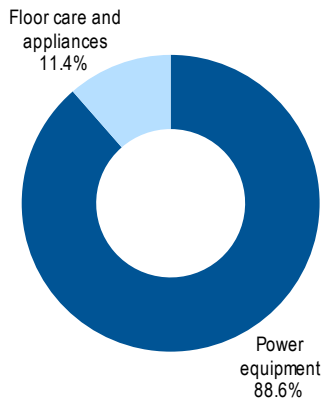
Source: the Company, Guotai Junan International.

Note:  
<sup>^</sup> Year of TTI's brand acquisition or licensing.  
 \* TTI uses AEG (a registered trademark of AB Electrolux (publ.)) and RYOBI (a registered trademark of Ryobi Limited) under license. All other trademarks are owned by TTI.

**TTI has been optimizing its global manufacturing diversification in response to changes in international trade relations.**

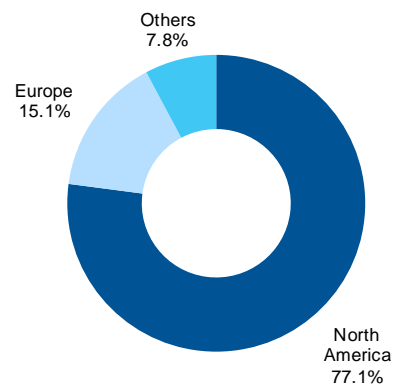
To stay close to the end market, branding centers of TTI's core brands are located in the US as North America is TTI's major market (generating 77.1% of TTI's 2019 revenue). In terms of production, TTI used to centralize its manufacturing capacity (around 70-80%) in China, with its core manufacturing base in Dongguan, Guangdong. In the face of uncertainty in global trade relations, TTI has been expanding its manufacturing facilities to Vietnam, Mexico and the US since 2018 and we estimate that by 2022-2023, nearly a half of TTI's products will be possibly manufactured outside China.

**Figure-2: TTI's Revenue Mix by Segment (2019)**



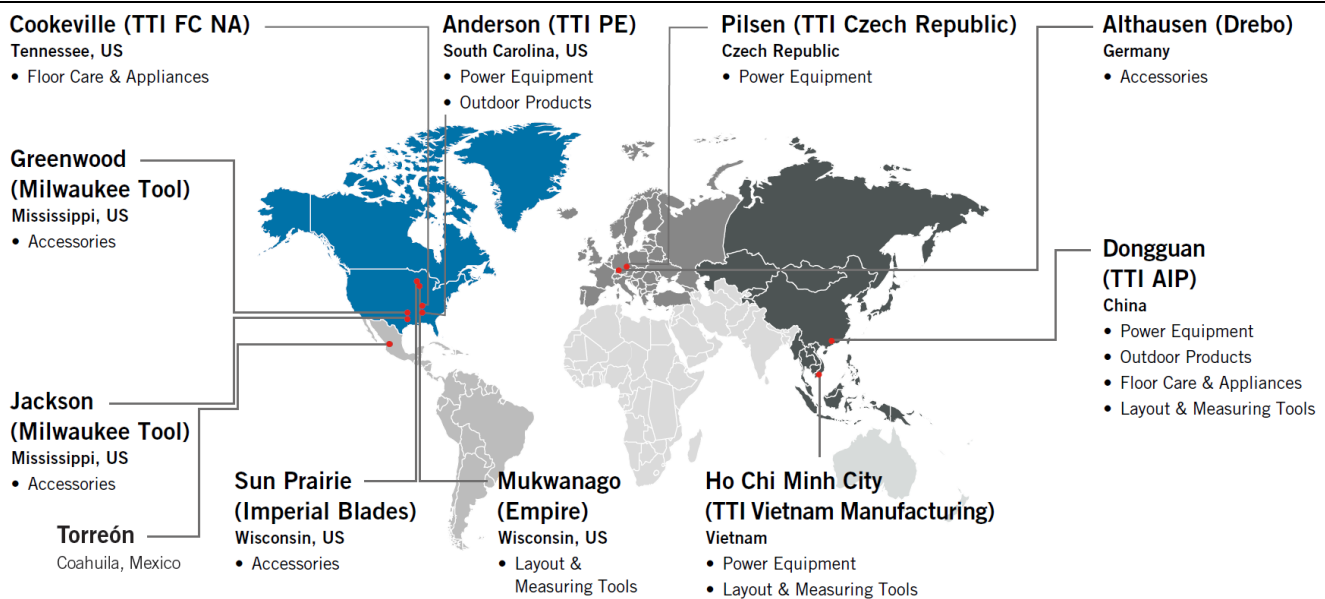
Source: the Company, Guotai Junan International.

**Figure-3: TTI's Revenue Mix by Region (2019)**



Source: the Company, Guotai Junan International.

**Figure-4: TTI's Global Manufacturing and Product Development Footprint**



Source: the Company, Guotai Junan International.

**Table-1: TTI's Major Directors and Shareholders**

#	Person	Position	Main Responsibility	Shareholding Ratio*
1	Horst Julius Pudwill	Chairman / Co-founder / Executive Director	Strategic planning and development	20.03%
2	Stephan Horst Pudwill	Vice Chairman / Executive Director	Managing, improving and monitoring internal operations	2.28%
3	Joseph Galli Jr	Chief Executive Officer / Executive Director	Integrating acquisitions and enhancing global sales potential	0.48%
4	Patrick Kin Wah Chan	Operations Director / Executive Director	Manufacturing operations	0.15%
5	Frank Chi Chung Chan	Chief Financial Officer / Executive Director	Corporate affairs and financial management	0.16%
6	Roy Chi Ping Chung	Non-executive Director / Co-founder / Former Vice Chairman	n.a.	4.73%
7	Camille Jojo	Non-executive Director	Participating in audit committee and remuneration committee	0.02%

Source: the Company, Guotai Junan International.

Note \*: shareholding ratio as at 30 June 2020.

POWER TOOLS

North America is expected to remain as the largest market of power tools. Based on Euromonitor's estimation, global sales of power tools will grow at a CAGR of 4.9% during 2019-2024. North America accounts for the largest share of global sales of power tools thanks to the popularity of DIY culture and lower population density. Despite great potential in emerging markets, we believe that North America will continue to lead the global power tools market in the incoming five years. Transition to cordless power tools has been accelerated by cheaper and lighter lithium batteries, but the penetration rate of cordless power tools in the US is still below 50%. We believe that the trend of upgrading to cordless power tools will continue to drive growth of power tools sales.

Figure-5: Global Sales of Power Tools by Region

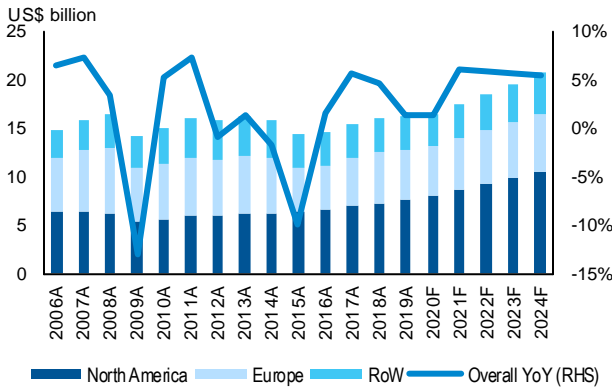
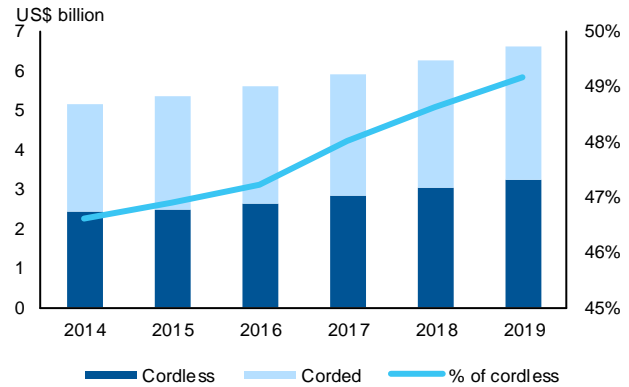


Figure-6: Penetration of Cordless Power Tools in the US

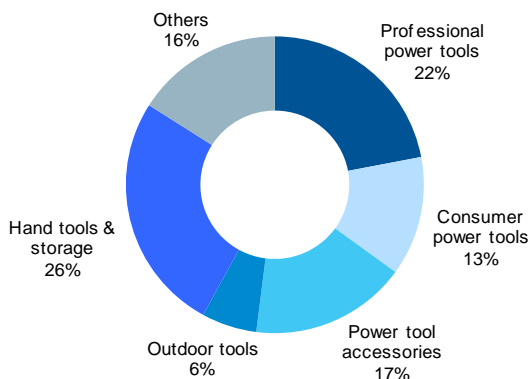


Source: Euromonitor, Guotai Junan International.

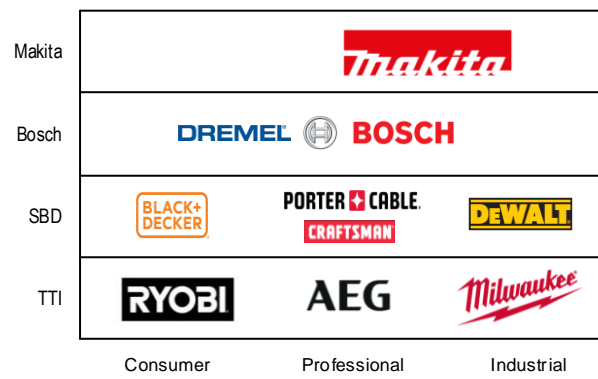
Source: Euromonitor, Guotai Junan International.

TTI's market share gains have been supported by organic growth driven by multi-brand strategy and cordless leadership. TTI has developed a comprehensive power tool brand portfolio: RYOBI specializes in affordable choices for DIY and garden hobbyists; AEG mainly targets professional tradesmen; and MILWAUKEE delivers advanced products for industrial and professional users in sectors including construction, transportation, energy, utilities, etc. We believe that TTI's multi-brand strategy provides the Company with advantages in catering for all levels of customers from various industries. In addition, since MILWAUKEE being the first to use lithium-ion batteries in its lines of cordless tools, TTI has been the most aggressive manufacturer in the transition from legacy power systems such as corded, pneumatic, hydraulic and gas to cordless. Thanks to its well-positioned branding and leading edge in cordless technology, TTI has tripled its market share in the past decade and become the world's second largest tool manufacturer in terms of sales of power tools, accessories and hand tools in 2019, according to Stanley Black & Decker (SBD, SWK US). We believe that the concentration ratio (CR4 in 2019: around 44%) of the power tool industry will continue to improve, given economies of scale and technological advantage of leading players. In comparison to SBD's M&A-driven growth, TTI's consecutive market share gains since 2008 were mainly on organic sales growth of its existing core brands. Overall, we expect that TTI will continue to win more market share on its well-positioned branding and strategic focus on cordless technology.

Figure-7: Global Tools & Storage Market Breakdown (2018) Figure-8: Brand Positioning of TTI and Other Leading Power Tool Manufacturers

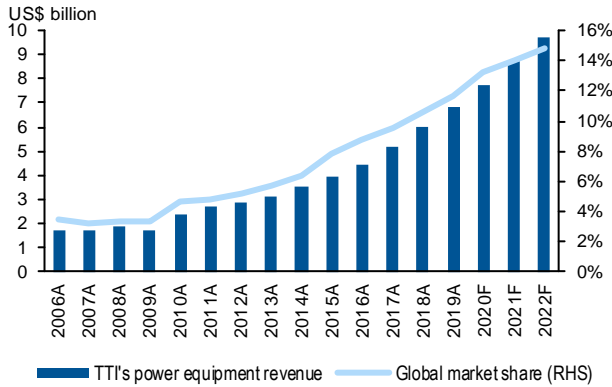


Source: SBD, Guotai Junan International.



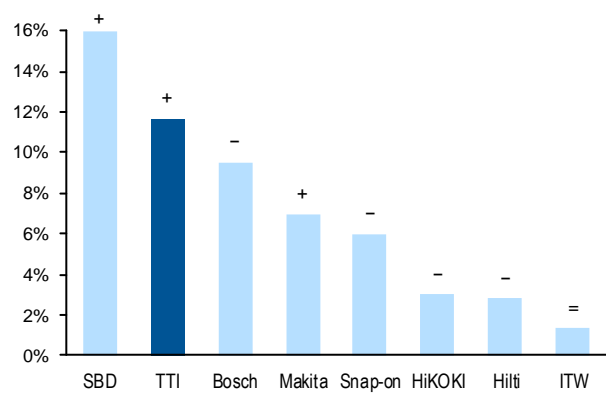
Source: the Company, SBD, Bosch, Makita, Guotai Junan International.

Figure-9: TTI's Global Market Share of Power Tools, Hand Tools and Garden Equipment



Source: the Company, Euromonitor, Guotai Junan International.

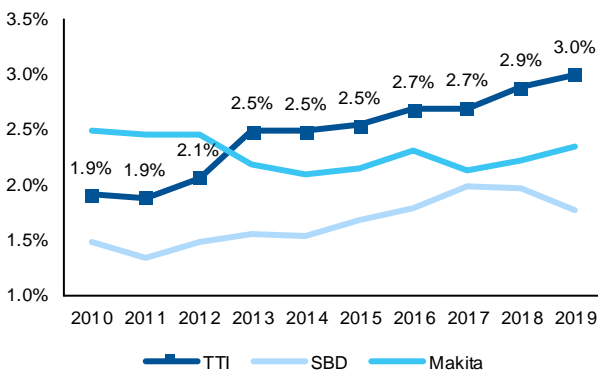
Figure-10: Global Tools and Storage Market Share of TTI and Other Leading Power Tool Manufacturers (2019)



Source: SBD, Guotai Junan International.  
Note: + increased; - decreased; = flat.

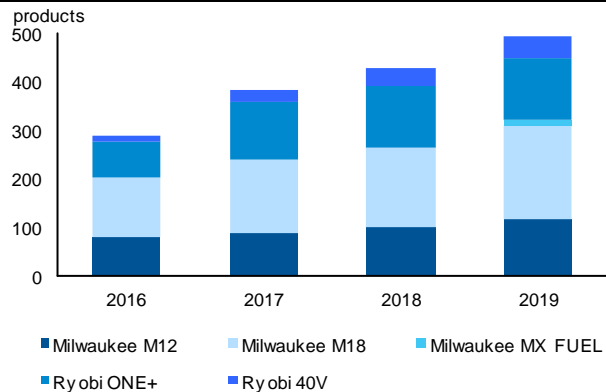
TTI's product competitiveness has been strengthened by consistently increasing R&D expenditure and rapidly expanding product family. After continuous aggressive investment in R&D in the past decade, TTI's R&D expense ratio hit a record high of 3.0% and significantly outpaced its peers. We believe that TTI will maintain an R&D expense ratio above 3% and put consistent effort into R&D to expand its cordless product family with more in-house technology advances in key components such as brushless motors, lithium battery packs and electronic control systems. TTI has developed leading universal battery platforms under its core brands, including M12, M18 and MX FUEL under MILWAUKEE, ONE+ and 40V under RYOBI, as well as ONEPWR under HOOVER and VAX, and maintained consistent compatibility for products on each of the platforms. For example, RYOBI ONE+ platform was launched in 1996 with NiCad batteries and then upgraded to lithium batteries in 2007, while new lithium batteries can be used in old tools and old NiCad batteries can still be used in newly launched tools. The universal battery platforms not only provide attractive choices of bare tools and replaceable batteries for TTI's customers, but also maintains customer loyalty to TTI's brands due to higher cross-brand switching costs as well as generation of recurring battery sales for TTI. We believe that the attractiveness of TTI's battery platforms will be continuously boosted by TTI's rapid expanding product family. In 2019, MILWAUKEE launched its new MX FUEL system and became a pioneer of introducing lithium batteries to high-output and heavy-duty tools, targeting to replace traditional powered light construction equipment (using gas, hydraulic or corded electric) with features including zero emissions and reduced noise and vibration. To illustrate the competitiveness of TTI's products, we conducted a cross-brand comparison on 1/2-inch cordless power drill, one of the most representative power tools. We believe that TTI's products strike good balance between cost and performance and stand out from competition with obvious advantages (in particular, strong torque and long warranty period in our comparison).

Figure-11: R&D Expense Ratios of TTI and Other Leading Power Tool Manufacturers











Source: the Company, Stanley Black & Decker, Makita, Guotai Junan International.

Figure-12: Compatible Products on TTI's Major Battery Platforms



Source: the Company, Guotai Junan International.

Table-2: Cross-Brand Comparison of Mainstream Products – 1/2-Inch Cordless Power Drill (18V/20V)

Company & Brand	TTI			Stanley Black & Decker			Bosch	Makita
	Milwaukee	Ryobi	DeWalt	Craftsman	Porter-Cable	Black+Decker		
Product image								
Model	2803	P214	DCD996	CMCD721	PCK607	BDCDHP220	GSR18V-535	XPH12
Motor type	Brushless	Brushed	Brushless	Brushless	Brushless	Brushed	Brushless	Brushless
Maximum speed (RPM)	2,000	1,600	2,000	2,100	1,800	1,500	1,900	2,000
Torque (inch/lbs.)	1,200	600	841 / 650 UWO <sup>(1)</sup>	400 UWO <sup>(1)</sup>	370 UWO <sup>(1)</sup>	412	535	530
Blows per minute	32,000	24,000	38,250	34,000	n.a.	n.a.	28,500	30,000
Weight (lbs.)	3.2	3.2	3.5	2.71	3.3	2.64	2.5	3.4
Warranty (year)	5	3	3	3	3	2	1	3
Price <sup>(2)</sup> (bare tool)	US\$139	US\$69	US\$159	US\$119	n.a.	n.a.	US\$149	US\$119
Price <sup>(2)</sup> (batteries incl.)	US\$279 (2-battery)	US\$139 (1-battery)	US\$299 (2-battery)	US\$179 (2-battery)	US\$139 (2-battery)	US\$95 (2-battery)	US\$199 (1-battery)	US\$197 (2-battery)

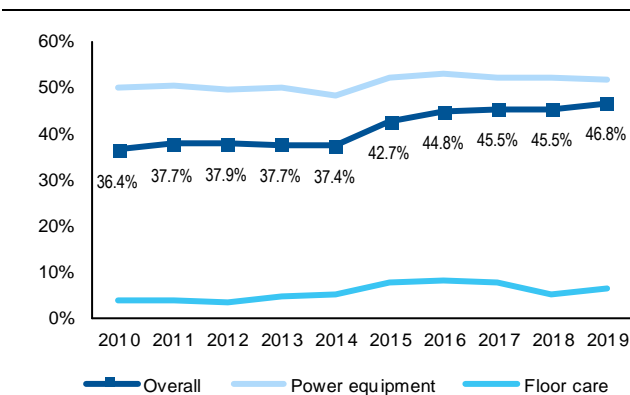
Source: the Company, SBD, Bosch, Makita, Home Depot, Lowe's, Guotai Junan International.

Note (1): UWO = Units Watts Out, a new power rating unit used by Stanley Black & Decker based on the drill's speed and torque output.

Note (2): List price at Home Depot or Lowe's without promotional discounts.

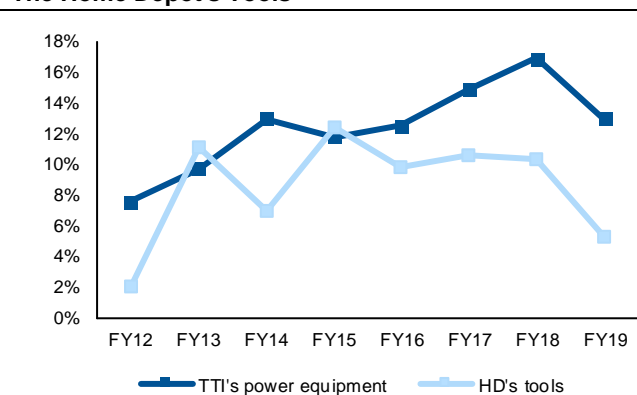
The Home Depot remains as TTI's most powerful distribution channel despite impact from online retailers and the COVID-19 pandemic. TTI has established close partnership with The Home Depot (HD), the largest home improvement retailer (also the No.1 power tool retailer) in North America, in forms of, for example, selling RYOBI products exclusively at The Home Depot. As TTI's largest distributor in the past decade, The Home Depot contributed 46.8% of TTI's total sales in 2019. As a proof of TTI's steady market gains in North America, growth of TTI's power equipment revenue outpaced that of The Home Depot's sales of tools in most years. In the US, specialty stores like The Home Depot has maintained their dominance with over 71% share of distribution channels of home improvement and gardening products during 2014-2019, barely impacted by fast-growing online retailers. Sales contribution from e-commerce was still relatively minor in 2019 (only 5.1%) due to customer demand for in-store services and high delivery costs. The Home Depot's online platforms contributed 9.3% of its total sales in FY19, higher than the market average, while around half of its online orders in the US were picked up in store instead of being delivered. On the other hand, because of the impact from the COVID-19 pandemic, The Home Depot's online sales surged 90.4% YoY in 1HFY20 and contributed 14.4% of total sales (FY19: 9.3%). In addition to strong online sales, The Home Depot's offline sales also recorded decent growth, leading to 15.9% YoY growth in total sales in 1HFY20. In fact, home improvement activities have increased in the US during the pandemic, since work-from-home arrangements provide homeowners with more time and boost their needs for home improvement projects. In general, we believe that TTI's sales growth in North America will be continuously supported by its strategic partnership with The Home Depot.

Figure-13: The Home Depot's Sales Contribution to TTI



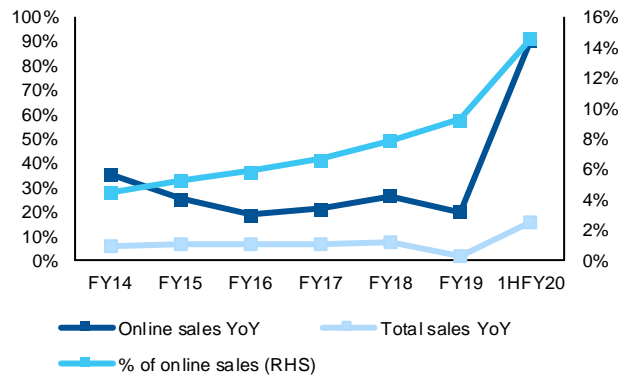
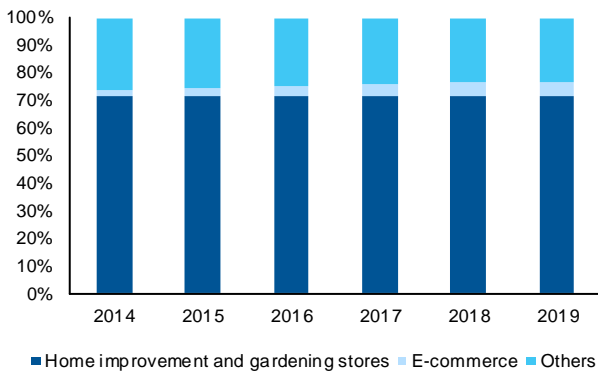
Source: the Company, Guotai Junan International.

Figure-14: Sales YoY Growth of TTI's Power Equipment vs. The Home Depot's Tools



Source: the Company, The Home Depot, Guotai Junan International.  
Note: Home Depot's fiscal years end by the Sunday nearest to 31<sup>st</sup> January.

Figure-15: Distribution Channel Mix of Home Improvement and Gardening Products in the US  
Figure-16: The Home Depot's Online Sales and Gardening Products in the US



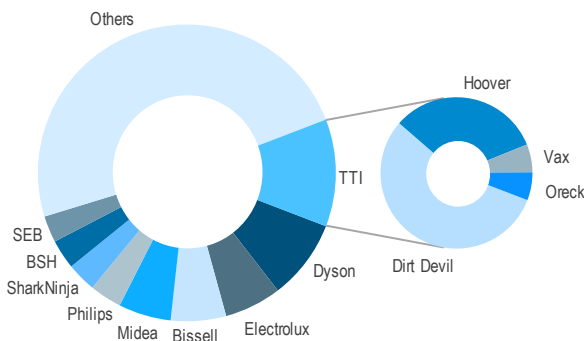
Source: Euromonitor, Guotai Junan International.

Source: The Home Depot, Guotai Junan International.

FLOOR CARE

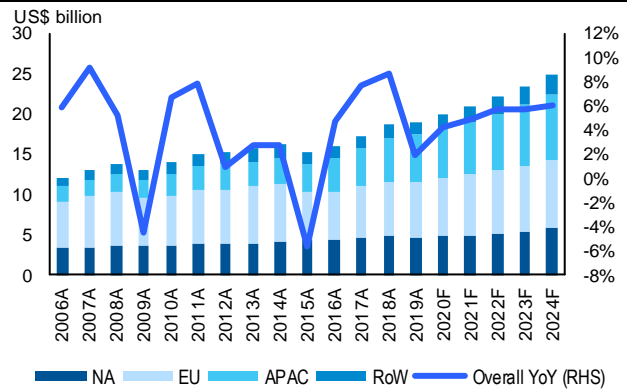
The turnaround in floor care is to be driven by new cordless and carpet washing products despite ongoing competition from robot vacuums. TTI has been leading the floor care market in North America and Europe with its powerful brands consisting of HOOVER, ORECK, VAX and DIRT DEVIL. Facing headwinds in the global floor care market since 2015, TTI has started to shift its strategic focus to cordless and carpet washing products and phase out low-margin corded products and OEM businesses. In June 2019, TTI launched its ONEPWR battery platform under HOOVER and VAX to leverage the success of battery platforms for power tools. Although we expect that competition in the floor care market will stay intense with competition from the fast-growing robot vacuum manufacturers, we believe that TTI's strategic shift towards cordless and carpet washing products is to be fruitful and will drive further improvement in the profit margin of its floor care businesses.

Figure-17: Global Market Share of Major Vacuum Manufacturers by Sales Volume (2019)



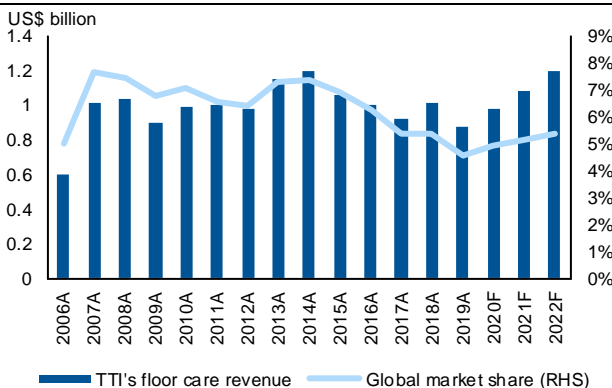
Source: Euromonitor, Guotai Junan International.

Figure-18: Global Sales of Vacuums by Region



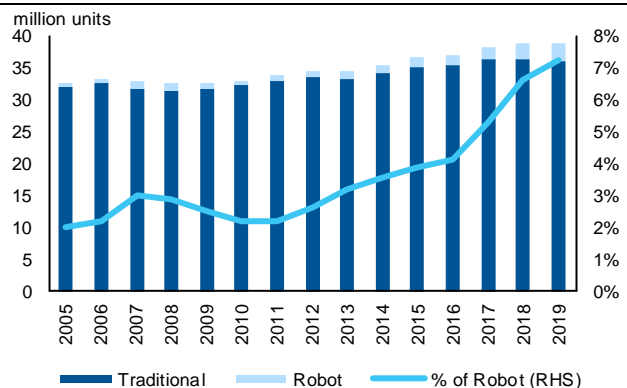
Source: Euromonitor, Guotai Junan International.

Figure-19: TTI's Global Floor Care Market Share



Source: the Company, Euromonitor, Guotai Junan International.

Figure-20: Sales Volume of Traditional vs. Robot Vacuums in North America



Source: Euromonitor, Guotai Junan International.

**EARNINGS FORECASTS AND FINANCIAL ANALYSIS**

**We expect TTI's total revenue to increase YoY by 14.0%/ 12.2% 11.4% in 2020/ 2021/ 2022, respectively.** In general, we believe that robust sales of power equipment will continue to drive TTI's revenue growth, while floor care and appliances will further recover after the strategic shift. Details on each segment are as follows:

- **Power equipment:** On the back of increasing R&D expenditure, we believe that TTI's market share gains are to be fueled by more aggressive expansion of new products on its leading battery platforms than most of its peers. Pioneer products such as the latest light equipment products on the MX FUEL platform are expected to accelerate TTI's sales expansion in more non-residential market segments, including oil and gas, industrial and infrastructure. Therefore, even if the positive effects from the COVID-19 pandemic on DIY demand fades away in the future, stronger demand from higher-end professional markets will support TTI's revenue growth momentum.
- **Floor care and appliances:** Thanks to the fruitful strategic transition, we expect TTI's floor care business to further recover with its competitive edge in battery platform plus its unique leadership in niche markets such as carpet washing. Given double-digit YoY growth rate outlook for revenue during 2020-2022, we believe that TTI is to recapture market share and maintain its leadership in spite of the increasing threat from robot vacuum manufacturers.

**Basic EPS forecasts for 2020/ 2021/ 2022 are US\$0.391/ US\$0.446/ US\$0.506, respectively.** Based on TTI's excellent proven record in the past decade plus bright outlook for TTI's ongoing product upgrades, we are confident in TTI's sustainable profit margin improvement. Details on each segment are as follows:

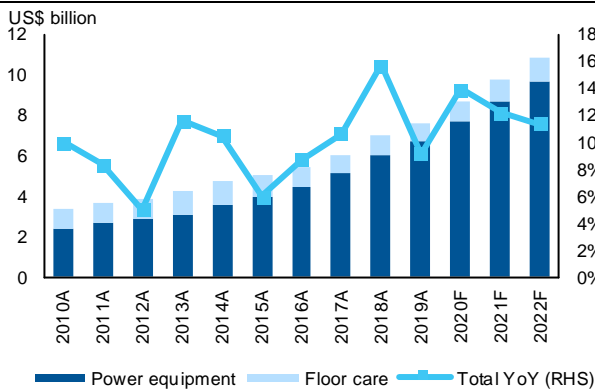
- **Power equipment:** Given fewer comparable products in the market, we expect that TTI's new products targeting high-end industrial and professional markets (e.g. light equipment products on the MX FUEL platform) will be more profitable and therefore steadily boost the profit margin of the segment by ongoing optimization of product mix.
- **Floor care and appliances:** Despite the highly competitive global floor care market, we expect that profit margin improvement of floor care and appliances will continue to be supported by better profitability of fast-growing cordless and carpet washing products as well as the phasing out of low-margin corded products.

**Table-3: Key Assumptions for Earnings Forecasts**

	2018A	2019A	2020F	2021F	2022F
<b>Revenue by segment (US\$ mn)</b>					
Power equipment	6,009	6,792	7,752	8,706	9,708
Floor care and appliances	1,012	875	990	1,103	1,219
<b>Operating margin by segment</b>					
Power equipment	10.0%	9.8%	10.0%	10.2%	10.3%
Floor care and appliances	0.9%	1.2%	1.4%	1.8%	2.2%
<b>Key financial data (US\$ mn)</b>					
Revenue	7,021	7,667	8,743	9,809	10,927
Gross profit	2,615	2,893	3,337	3,781	4,253
Shareholders' profit	552	615	716	817	929
Basic EPS (US\$)	0.302	0.337	0.391	0.446	0.506

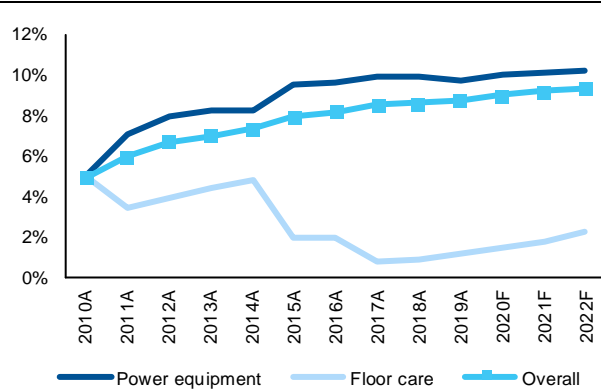
Source: the Company, Guotai Junan International.

**Figure-21: TTI's Revenue by Segment**



Source: the Company, Guotai Junan International.

**Figure-22: TTI's Operating Margin by Segment**

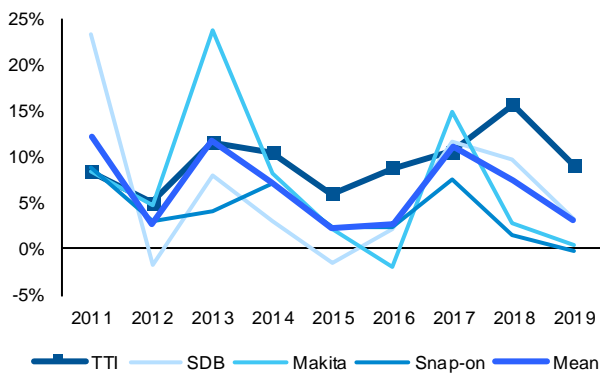


Source: the Company, Guotai Junan International.



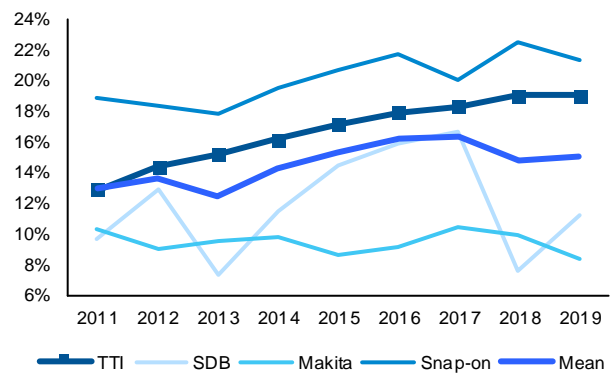
**Outstanding ROE has been supported by high asset turnover with ongoing improvement in profit margin.** TTI has maintained higher-than-average revenue growth in most of the past eight years with a CAGR of 9.5% during 2010-2019, which beat all its major peers and accounted for its steady market share gains. In addition to the outperforming revenue growth, TTI's ROE has been rising consecutively and consistently outperformed SDB and Makita (6586 JP), and was only second to Snap-on (SNA US). Based on our DuPont analysis, we believe that TTI's outstanding ROE could be mainly attributable to TTI's top-tier asset turnover, which demonstrated the Company's excellence in overall operating efficiency. Compared with its peers, TTI has been moderately leveraged with a net gearing ratio of only 0.5% as at the end of 2019. Despite the underperformance in most years, TTI's gross margin and net margin has been continuously improving on product mix optimization as well as economies of scale thanks to rapid top-line growth, playing as the largest driver of rising ROE. Coupled with steady profit growth, TTI has been consecutively raising its dividend payout ratio since 2012. We expect TTI's dividend CAGR to be 18.0% during 2019-2022 and TTI's dividend payout ratio to reach 45% by 2022, bolstered by robust operating cash inflows.

**Figure-23: Revenue Growth of TTI and Its Major Peers**



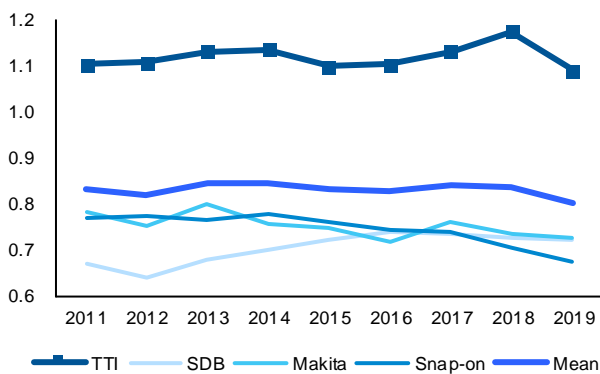
Source: the Company, SDB, Makita, Snap-on, Guotai Junan International.  
Note: Fiscal years of Makita are ended by 31<sup>st</sup> March.

**Figure-24: ROE of TTI and Its Major Peers**



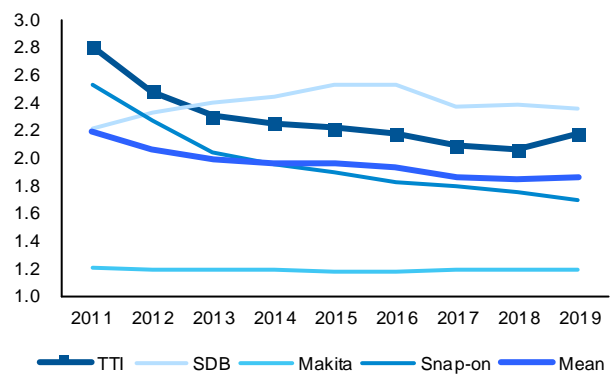
Source: the Company, SDB, Makita, Snap-on, Guotai Junan International.

**Figure-25: Asset Turnover of TTI and Its Major Peers**



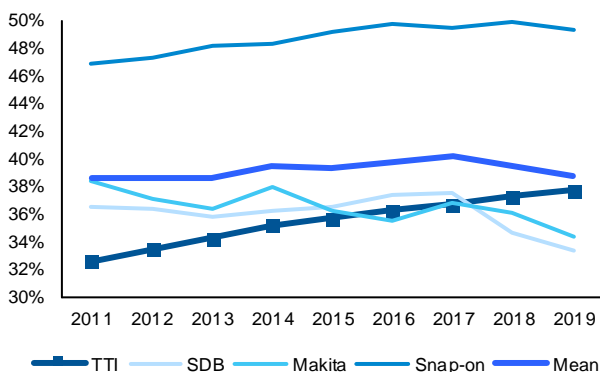
Source: the Company, SDB, Makita, Snap-on, Guotai Junan International.

**Figure-26: Equity Multiplier of TTI and Its Major Peers**



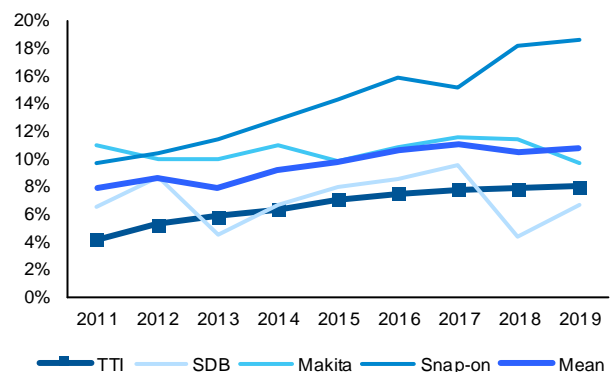
Source: the Company, SDB, Makita, Snap-on, Guotai Junan International.

**Figure-27: Gross Margin of TTI and Its Major Peers**



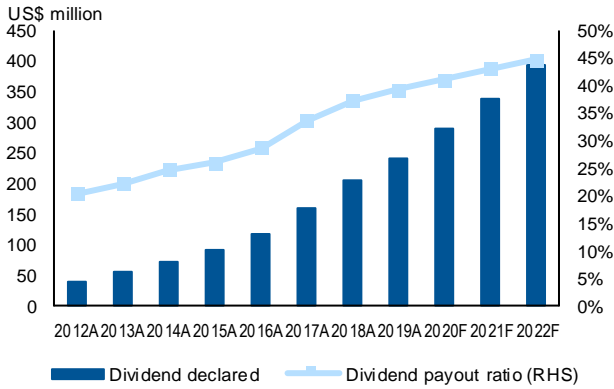
Source: the Company, SDB, Makita, Snap-on, Guotai Junan International.

**Figure-28: Net Margin of TTI and Its Major Peers**



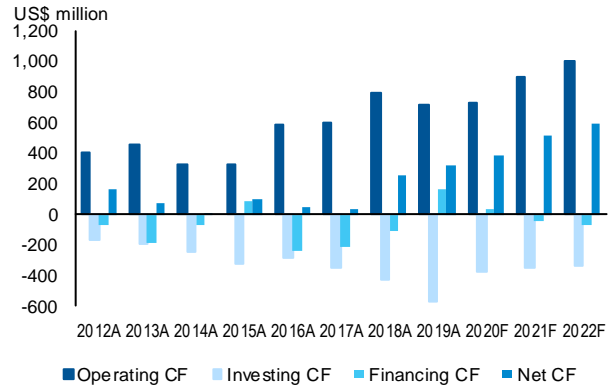
Source: the Company, SDB, Makita, Snap-on, Guotai Junan International.

**Figure-29: TTI's Dividend Payout**



Source: the Company, Guotai Junan International.

**Figure-30: TTI's Cash Flow**



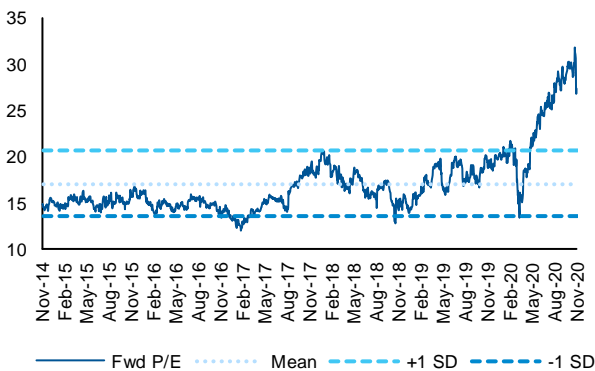
Source: the Company, Guotai Junan International.

**VALUATION AND RECOMMENDATION**

**Initiate with "Accumulate" and a target price of HK\$119.30.** We derived our target price from DCF valuation assuming a perpetual growth rate of 2.5% and a WACC of 6.73% derived from a cost of equity of 8.08%, a cost of debt of 3.60%, and a target debt/equity ratio of 40%. Our cost of equity of 8.08% is based on a risk-free rate of 0.69%, a market risk premium of 8.21% and a beta of 0.9 (5-year weekly mean on Bloomberg). Despite that both PE ratio and PB ratio of the Company hit 10-year record highs, resulting in trading at a valuation premium over other leading power tool manufacturers, we believe that TTI's valuation premium could be justified by its higher certainty in consistent improvement in both market share and profit margin that are further tested by the challenging environment due to the COVID-19 pandemic. Despite that valuation of TTI may face some short-term pressure due to potential reduction in DIY demand once the COVID-19 pandemic is controlled by vaccines, we expect TTI to continuously strengthen its leadership by consistent R&D expenditures and strategic shift towards more profitable segments in industrial and professional equipment markets. Our target price of HK\$119.30 represents 39.1x/ 34.3x/ 30.2x 2020-2022 PE ratio and 7.3x 2020 PB ratio. We initiate coverage on TTI with an investment rating of "Accumulate".

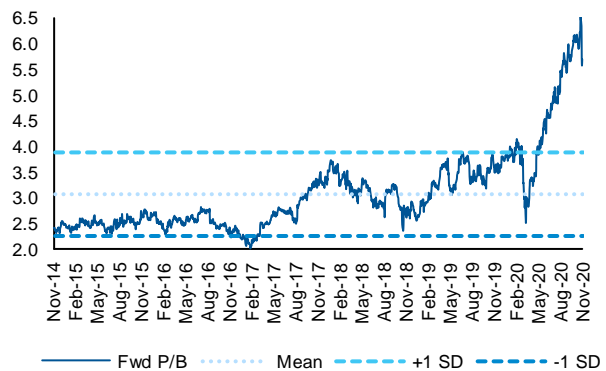
**Key risk factors:** 1) sluggishness of home improvement and construction activities in the US; 2) reduction in technology leadership due to R&D failures; 3) deterioration of global trade environment; 4) increasing reliance on one strong distributor; and 5) rising raw material costs for brushless motors, lithium battery packs and other key components.

**Figure-31: TTI's 12-Month Forward PE Ratio**



Source: Bloomberg, Guotai Junan International.

**Figure-32: TTI's 12-Month Forward PB Ratio**



Source: Bloomberg, Guotai Junan International.

**Table-4: Peers Comparison**

Company	Stock Code	Currency	Last Price	Market Cap (HKD mn)	PE (fiscal year)				PB (fiscal year)				ROE(%)	D/Y(%)	EV/EBITDA
					19A	20F	21F	22F	19A	20F	21F	22F	20F	20F	20F
<b>Global Listed Peers</b>															
Techtronic Industries Co Ltd	669 HK	HKD	97.450	182,316	36.9	31.8	26.2	21.8	6.7	5.9	5.5	4.5	19.8	1.2	20.9
Stanley Black & Decker Inc	SWK US	USD	180.890	224,738	28.1	21.4	19.1	17.0	3.6	2.7	2.5	2.3	13.8	1.5	13.3
Makita Corp	6586 JP	JPY	5,230.000	105,359	25.5	29.7	30.7	27.3	2.5	2.5	2.4	2.2	8.3	1.6	9.8
Snap-on Inc	SNA US	USD	170.180	71,542	13.5	15.9	14.8	14.3	2.7	2.5	2.3	2.1	16.8	2.6	10.8
Husqvarna AB-B	HUSQB SS	SEK	89.260	46,080	20.2	17.6	16.4	14.8	3.0	2.8	2.5	2.3	14.3	2.6	9.8
SEB SA	SK FP	EUR	145.000	66,643	19.0	24.7	17.4	15.6	3.0	2.8	2.5	2.2	11.8	1.0	11.8
Electrolux AB-Series B	ELUXB SS	SEK	205.900	57,081	23.6	16.4	14.1	11.6	2.6	2.6	2.3	2.1	16.8	3.8	6.8
JS Global Lifestyle Co Ltd	1691 HK	HKD	15.080	53,942	50.6	26.1	19.0	14.6	5.1	4.9	4.0	3.3	18.9	0.7	14.9
iRobot Corp	IRBT US	USD	76.390	16,661	25.1	21.6	35.6	20.6	3.3	2.7	2.7	2.5	14.2	0.0	9.0
Nilfisk Holding A/S	NLFSK DC	DKK	105.600	3,515	44.2	42.3	12.3	9.3	2.4	2.5	2.1	1.8	1.7	0.8	10.1
Simple Average					28.7	24.8	20.6	16.7	3.5	3.2	2.9	2.5	13.6	1.6	11.7
Weighted Average					28.4	24.4	21.4	18.4	4.0	3.5	3.2	2.8	15.0	1.6	13.5
<b>Mainland China Listed Peers</b>															
Hang Zhou Great Star Industrial-A	002444 CH	CNY	26.370	33,826	31.4	23.2	19.3	16.4	3.8	3.3	2.9	2.5	14.8	0.9	18.0
Shanghai Worth Garden Co Ltd-A	300483 CH	CNY	35.620	6,111	49.3	11.1	n.a.	n.a.	2.1	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Ken Holding Co Ltd-A	300126 CH	CNY	10.670	3,844	355.7	n.a.	n.a.	n.a.	3.3	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Beijing Roborock Technology-A	688169 CH	CNY	850.410	68,043	54.3	47.6	38.5	32.8	28.6	10.9	8.7	7.0	29.6	0.6	n.a.
Ecovacs Robotics Co Ltd-A	603486 CH	CNY	65.750	45,052	298.9	89.1	57.4	47.8	14.9	12.9	11.0	9.6	13.9	0.3	n.a.
KingClean Electric Co Ltd-A	603355 CH	CNY	35.830	17,599	28.7	26.4	23.0	21.3	4.5	4.1	3.6	3.3	15.6	0.9	n.a.
Simple Average					136.4	39.5	34.5	29.6	9.5	7.8	6.6	5.6	18.5	0.7	18.0
Weighted Average					116.9	50.2	38.1	32.3	16.3	9.2	7.6	6.4	20.8	0.6	18.0

Source: Bloomberg, Guotai Junan International.

**Financial Statements and Ratios**

Income Statement						Balance Sheet					
Year end 31 Dec (US\$ m)	2018A	2019A	2020F	2021F	2022F	Year end 31 Dec (US\$ m)	2018A	2019A	2020F	2021F	2022F
Total revenue	7,021	7,667	8,743	9,809	10,927	Property, plant and equipment	791	1,087	1,117	1,102	1,077
Cost of sales	(4,407)	(4,774)	(5,405)	(6,027)	(6,674)	Intangible assets	621	667	704	736	763
Gross profit	2,615	2,893	3,337	3,781	4,253	Goodwill	581	581	581	581	581
Other income	7	11	13	16	20	Others non-current assets	131	340	306	259	202
Selling expenses	(1,103)	(1,195)	(1,370)	(1,546)	(1,734)	Total non-current assets	2,124	2,674	2,707	2,678	2,623
Administrative expenses	(708)	(805)	(927)	(1,047)	(1,172)	Inventories	1,767	2,113	2,533	2,958	3,412
R&D expenses	(203)	(230)	(262)	(300)	(343)	Trade & other receivables	1,127	1,229	1,504	1,703	1,891
Operating profit	607	673	791	905	1,024	Cash & cash equivalents	1,104	1,412	1,796	2,318	2,933
Finance costs, net	(13)	(12)	(23)	(27)	(26)	Other current assets	228	271	311	350	401
Share of results of associates	0	0	1	1	1	Total current assets	4,225	5,024	6,144	7,328	8,637
Profit before tax	595	661	770	879	999	Total assets	6,349	7,698	8,851	10,006	11,260
Income tax	(42)	(46)	(54)	(61)	(70)	Trade & other payables	1,921	2,177	2,555	2,900	3,273
Profit after tax	553	615	716	817	929	ST borrowings	499	741	883	1,007	1,126
Non-controlling interest	(0)	(0)	(0)	(0)	(0)	Other current liabilities	196	299	313	325	348
Shareholders' profit / loss	552	615	716	817	929	Total current liabilities	2,616	3,218	3,750	4,233	4,746
Basic EPS	0.302	0.337	0.391	0.446	0.506	LT borrowings	540	755	918	1,061	1,204
						Other non-current liabilities	135	331	336	361	406
						Total non-current liabilities	676	1,086	1,254	1,422	1,610
						Total liabilities	3,292	4,304	5,004	5,654	6,356
						Share capital	655	662	668	672	676
						Reserves	2,403	2,732	3,179	3,680	4,228
						Total shareholders' equity	3,058	3,395	3,847	4,352	4,904
						Minority interest	(0)	(0)	(0)	(0)	0
						Total equity	3,057	3,394	3,847	4,352	4,904
						Total equity & liabilities	6,349	7,698	8,851	10,006	11,260
Cash Flow Statement						Financial Ratios					
Year end 31 Dec (US\$ m)	2018A	2019A	2020F	2021F	2022F		2018A	2019A	2020F	2021F	2022F
Profit before tax	595	661	770	879	999	Gross margin (%)	37.2	37.7	38.2	38.6	38.9
Depreciation & amortization	242	325	372	405	435	Operating margin (%)	8.7	8.8	9.1	9.2	9.4
Changes in working capital	(30)	(255)	(308)	(273)	(263)	Net margin (%)	7.9	8.0	8.2	8.3	8.5
Income tax paid	(85)	(87)	(105)	(127)	(146)	ROE (%)	19.1	19.1	19.8	19.9	20.1
Other adjustments	72	79	10	25	20	ROA (%)	9.8	9.4	9.4	9.4	9.5
Cash from operating activities	794	724	739	909	1,044	Dividend payout ratio (%)	37.5	39.5	41.4	43.2	45.0
Capital expenditure	(395)	(616)	(399)	(383)	(397)	Net gearing ratio (%)	Net cash	0.5	Net cash	Net cash	Net cash
Other investing activities	(29)	47	20	37	57	Interest coverage ratio (x)	16.6	13.6	12.7	12.6	12.6
Cash from investing activities	(424)	(568)	(379)	(346)	(340)						
Net changes in borrowings	(30)	692	307	270	263						
Dividends paid	(183)	(224)	(262)	(320)	(380)						
Other financing activities	107	(305)	(16)	5	29						
Cash from financing activities	(106)	163	30	(46)	(88)						
Cash at beg of year	864	1,104	1,412	1,796	2,318						
Net changes in cash	264	319	390	517	615						
Effect of exchange rate changes	(24)	(11)	(6)	5	0						
Cash at End of Year	1,104	1,412	1,796	2,318	2,933						

Source: the Company, Guotai Junan International.

**Company Rating Definition**

The Benchmark: Hong Kong Hang Seng Index

Time Horizon: 6 to 18 months

Rating		Definition
Buy	买入	Relative Performance >15%; or the fundamental outlook of the company or sector is favorable.
Accumulate	收集	Relative Performance is 5% to 15%; or the fundamental outlook of the company or sector is favorable.
Neutral	中性	Relative Performance is -5% to 5%; or the fundamental outlook of the company or sector is neutral.
Reduce	减持	Relative Performance is -5% to -15%; or the fundamental outlook of the company or sector is unfavorable.
Sell	卖出	Relative Performance <-15%; or the fundamental outlook of the company or sector is unfavorable.

**Sector Rating Definition**

The Benchmark: Hong Kong Hang Seng Index

Time Horizon: 6 to 18 months

Rating		Definition
Outperform	跑赢大市	Relative Performance >5%; or the fundamental outlook of the sector is favorable.
Neutral	中性	Relative Performance is -5% to 5%; or the fundamental outlook of the sector is neutral.
Underperform	跑输大市	Relative Performance <-5%; or the fundamental outlook of the sector is unfavorable.

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