

## Airtac International Group (1590.TW): A new cycle starts; TP up to NT\$1,400 (Buy on CL)

Key takeaways from AirTAC's 4Q22 earnings call we hosted today include:

1. For 2023 guidance, AirTAC expects its revenue to grow by double digits % YoY (driven by both pneumatic and linear guide business) with 30%+ OPM (the actual number could be higher, which depends on the company's product shipment volume and pricing).
2. AirTAC expects its revenue will see strong growth from 2Q23 given the much earlier than expected easing of COVID controls with normal peak season for pneumatic, and the company expects its 2H23 revenue can be higher than 1H23 mainly driven by more back-end loaded linear guide revenue performance.
3. AirTAC believes the China pneumatic market size will grow by single digits % YoY in 2023, after the double digits % YoY market size decline in 2022; moreover, the company expects its pneumatic revenue can outgrow the market by double digits % YoY again in 2023.
4. AirTAC believes battery and energy lighting etc environment friendly industries should continue to be the strongest growing markets in 2023, with government support. Moreover, the company expects to see better market share in the auto industry and believes the model/spec upgrading demand will drive their electronics revenue in 2023.
5. AirTAC's days of inventory reached 160 days target in end of 2022, and the company will further increase its UTR to 110% (from 100% now) to fulfill the strong 2Q23 market demand.
6. AirTAC expects its linear guide revenue can reach RMB600mn in 2023 (vs. RMB180mn in 2022), with increasing capacity (annual capacity will expand to RMB2bn by March 2023 vs. RMB1bn in end of 2022) and much loosen government COVID control policy.
7. AirTAC targets to acquire 30-40% of total China linear guide market share in the next 8-10 years, which suggest RMB5-6bn annual linear guide revenue, with competitive pricing strategy (20-30% lower than peers now, which could further widen in coming years once capacity expands, as per our view) and high production efficiency.
8. Most AirTAC's material cost had decreased 20% from the peak level in April/May

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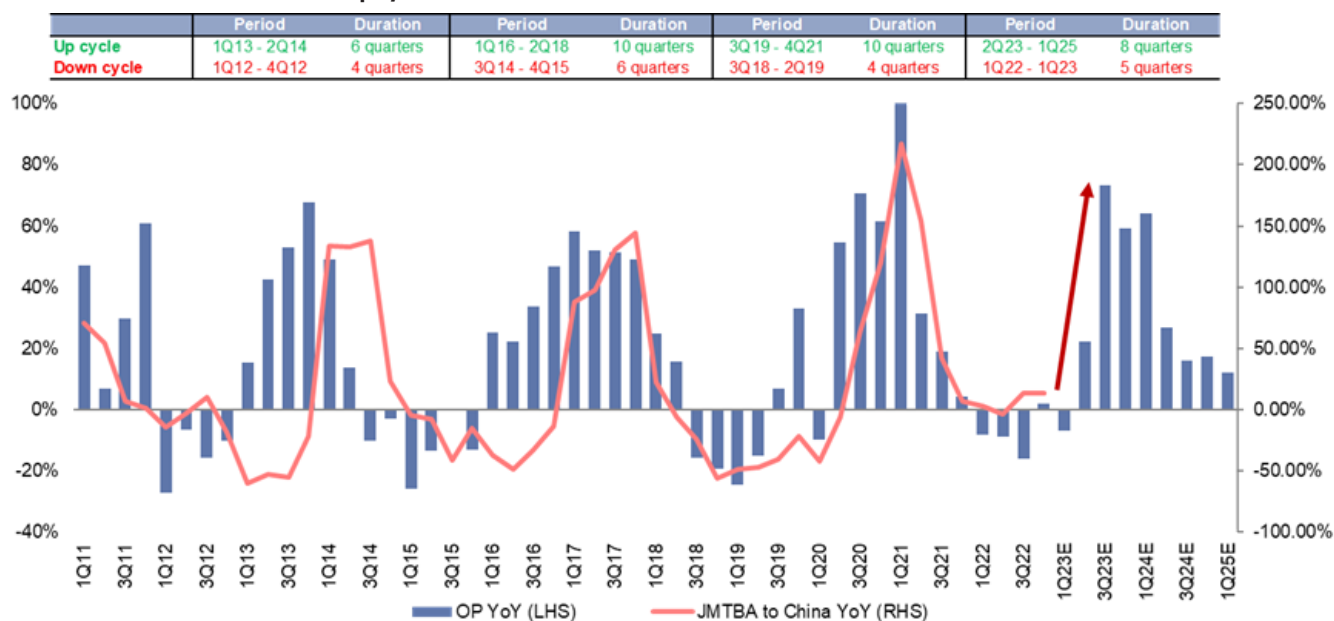
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2022 to early Dec 2022 and remain flat since then, which the company expects will benefit its margin level (material accounts for 40-50% of pneumatic COGS) in 2023, as the company has no plan to revise down their product pricing.

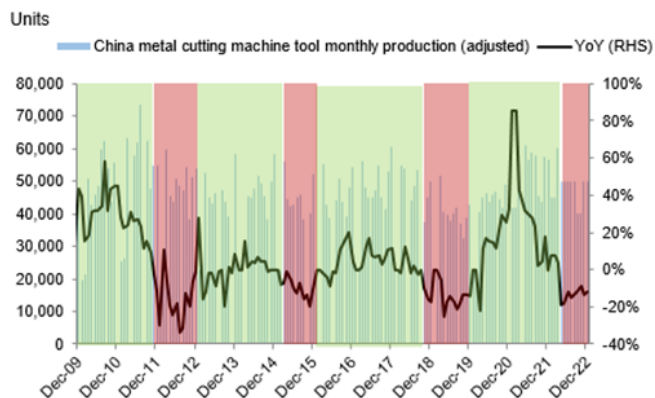
Overall, we find mgmt's comments regarding demand, profitability and cycle quite positive. We expect AirTAC to start a new round of up cycle by 2Q23 supported by cyclical demand recovery post China reopening as well as structural growth tailwinds from renewable energy related segments (battery, energy lighting etc). As per historical pattern, AirTAC's up cycle should last for 8-10 quarters ([Exhibit 1](#)) and we believe this upcoming up cycle should be no exception. In other words, the up cycle should last at least until 1Q25 in our view (as compared to mgmt's thoughts that this cycle should sustain longer than historical average duration due to rising labor shortages and manufacturing upgrade etc). For the near term, we expect AirTAC's Feb sales of NT\$1,982/RMB443mn (36% MoM, 15/13% YoY) with daily sales of RMB19.2 mn (similar to Jan) as their customers gradually get back to work from CNY holidays. We expect its sales to pick up more notably from March ([Exhibit 5](#)) and 2H23 to be stronger than 1H23 thanks to more resilient core business momentum as well as rising contribution from linear guide.

**Exhibit 1: AirTAC at the start of a new up cycle**



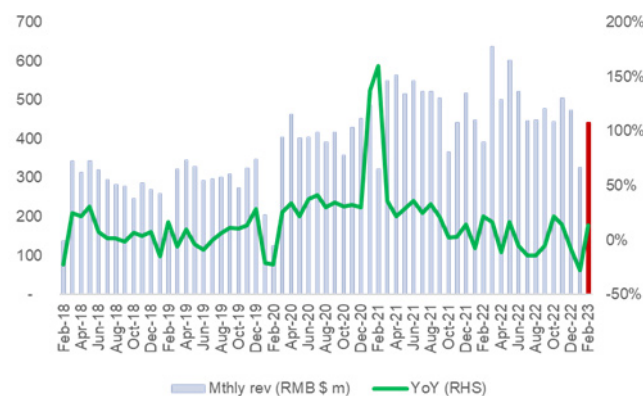
Source: Company data, Goldman Sachs Global Investment Research

**Exhibit 2: China metal cutting machine tool cycles (Green: upcycle; Red: Downcycle)**



Source: Company data

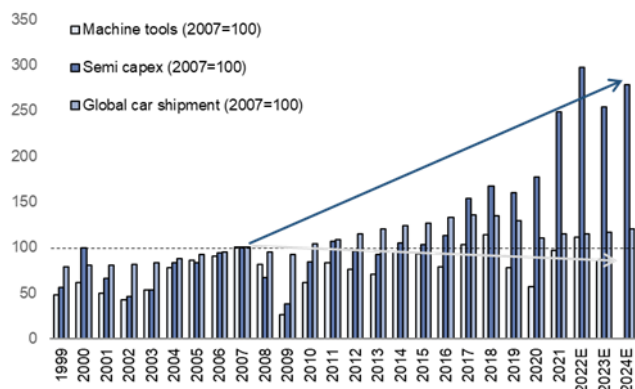
**Exhibit 4: We now expect AirTAC Feb revenue will reach RMB443mn (36% MoM, 13% YoY)**



Source: Company data, Goldman Sachs Global Investment Research

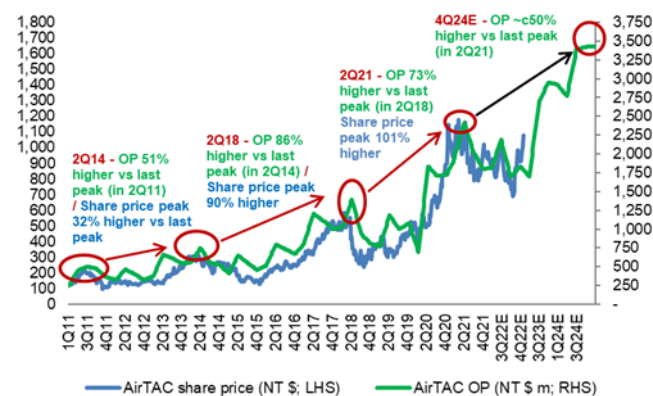
**Exhibit 6: Semi and machine tool slowing down in 2023 while auto more resilient helped by EV**

Japan machine tool orders vs. SPE capex vs. global car shipments



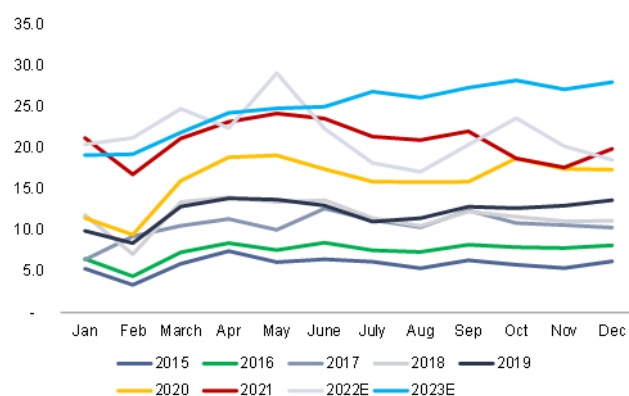
Source: Company data, Goldman Sachs Global Investment Research, JMTBA, SEMI

**Exhibit 3: We believe the most critical share price driver for AirTAC is its earnings trend over the long term**



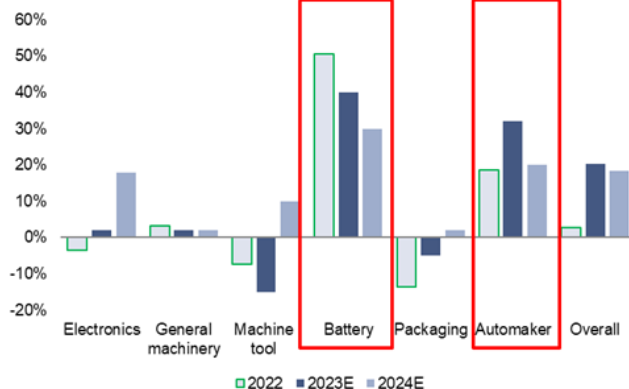
Source: Company data, Goldman Sachs Global Investment Research

**Exhibit 5: AirTAC's daily revenue trend (RMB mn) to see better YoY improvement from 2023 after COVID control measures ease**

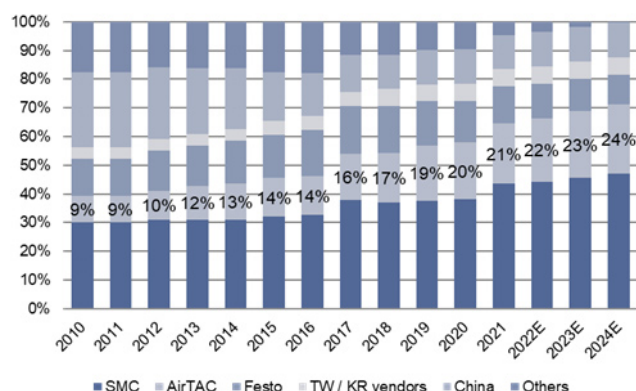


Source: Company data, Goldman Sachs Global Investment Research

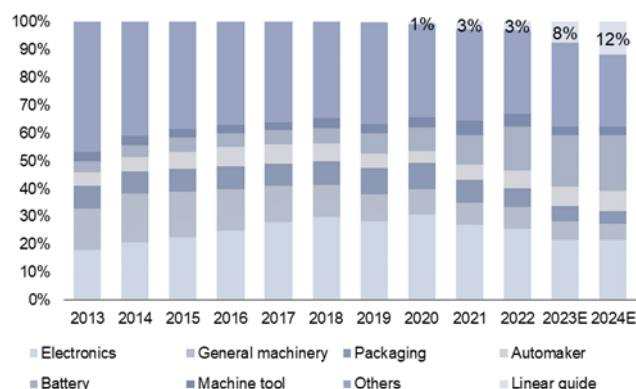
**Exhibit 7: AirTAC's revenue growth by segment - we expect battery and automaker to see better growth in coming years**



Source: Company data, Goldman Sachs Global Investment Research

**Exhibit 8: We expect AirTAC's China pneumatic market share will continue to grow in coming years**

Source: Company data, Goldman Sachs Global Investment Research

**Exhibit 9: We estimate AirTAC's linear guide revenue contribution will accelerate from 2023E**

Source: Company data, Goldman Sachs Global Investment Research

### 4Q22 review

AirTAC's 4Q22 revenue was in line with GSe but 1% lower than BBG consensus, given the slower China pneumatic demand in December due to COVID outbreak in China, while the company's 4Q22 GM was 0.1ppt lower than GSe/BBG consensus with slightly lower than expected scale for linear guide business. For OPM, 4Q22 actual number is 1.1/0.3ppt higher than GSe/BBG consensus mainly due to the company's greater than expected efficiency on strong cost control. Moreover, tax rate is lower than our estimate which results in a 14% higher than GSe net income in 4Q22, but which is 7% lower than BBG consensus due to the unexpected non-OP loss (mainly driven by unfavorable FX movement and high interest expense) in 4Q22.

**Exhibit 10: AirTAC's 4Q22 comp table**

AirTAC (1590.TW)	4Q22			QoQ		YoY		Bloomberg consensus	
P&L (NT\$m)	Actual	GS est.	Diff (%)	3Q22	QoQ	4Q21	YoY	Consensus	%
Revenue	6,265	6,279	0%	6,078	3%	5,768	9%	6,350	-1%
Gross profits	2,905	2,919	-1%	2,814	3%	2,726	7%	2,948	-1%
Operating profits	1,836	1,770	4%	1,704	8%	1,801	2%	1,841	0%
Pre-tax income	1,759	1,835	-4%	1,802	-2%	2,065	-15%	1,869	-6%
Net earnings	1,342	1,179	14%	1,391	-4%	1,606	-16%	1,439	-7%
EPS, NT\$	6.71	5.90	14%	6.96	-4%	8.10	-17%	7.11	-6%
Gross margin (%)	46.4%	46.5%	-0.1ppt	46.3%	0.1ppt	47.3%	-0.9ppt	46.4%	-0.1ppt
EBIT margin (%)	29.3%	28.2%	1.1ppt	28.0%	1.3ppt	31.2%	-1.9ppt	29.0%	0.3ppt
Net margin (%)	21.4%	18.8%	2.6ppt	22.9%	-1.5ppt	27.8%	-6.4ppt	22.7%	-1.2ppt

Source: Company data, Goldman Sachs Global Investment Research, Bloomberg

### Earnings revisions

We revise up AirTAC 2023/24/25E earnings estimate by 5/8/6% to factor in (1) stronger topline growth from electronics/general manufacturing supported by replacement demand (revise up 2023/24/25E revenue estimate by 2/5/3%) and (2) more solid operating leverage which is more notable during up-cycles (which leads to 0.7/1.1/1.1ppt higher OPM in 2023/24/25E).

**Exhibit 11: Earnings revisions summary**

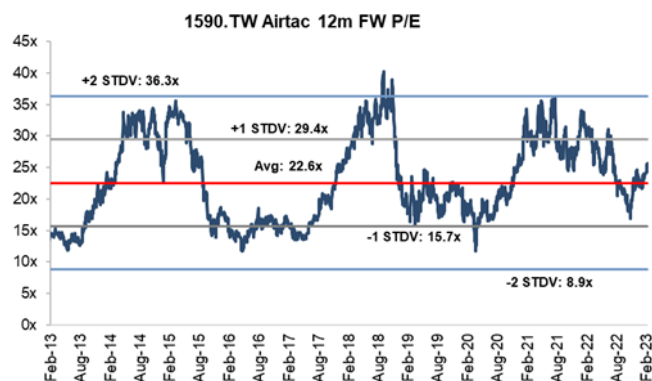
AirTAC P&L ( NT\$ mn)	2023E New	2023E Old	Diff.	2024E New	2024E Old	Diff.	2025E New	2025E Old	Diff.
Sales	31,339	30,669	2%	37,096	35,313	5%	40,187	39,049	3%
Gross Profit	15,133	14,691	3%	18,245	17,252	6%	19,987	19,371	3%
EBIT	10,235	9,813	4%	13,005	11,991	8%	14,441	13,592	6%
Net Income	8,307	7,899	5%	10,263	9,518	8%	11,430	10,742	6%
<b>EPS (NT\$)</b>	<b>41.54</b>	<b>39.50</b>	<b>5%</b>	<b>51.32</b>	<b>47.59</b>	<b>8%</b>	<b>57.15</b>	<b>53.71</b>	<b>6%</b>
<b>Ratio analysis</b>									
Gross margin	48.3%	47.9%	0.4pp	49.2%	48.9%	0.3pp	49.7%	49.6%	0.1pp
EBIT margin	32.7%	32.0%	0.7pp	35.1%	34.0%	1.1pp	35.9%	34.8%	1.1pp
Net margin	26.5%	25.8%	0.8pp	27.7%	27.0%	0.7pp	28.4%	27.5%	0.9pp

Source: Goldman Sachs Global Investment Research

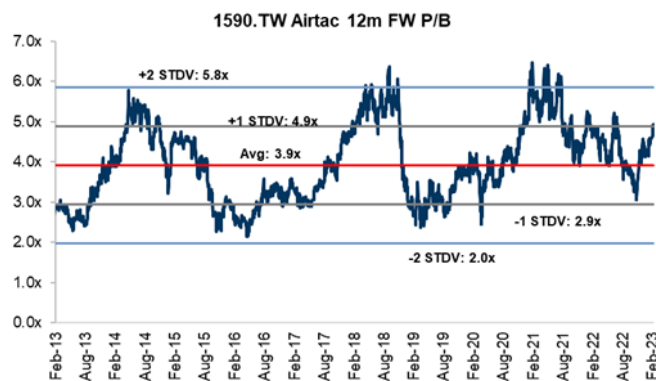
**Valuation and risks**

We revise up our target PE multiple from 28x to 30x, to factor in the early upcycle outlook, where we believe AirTAC should benefit from the China industrial demand uptrend earlier than other industrial players considering pneumatic is a short lead time (generally <1 week for AirTAC) product with limited supply chain inventory. The new 30x PE multiple target is in line with past few upcycle valuation (30-35+ $\times$ ; [Exhibit 12](#)) which is 1.1 s.d. higher than the past 10-year average of 22.6x.

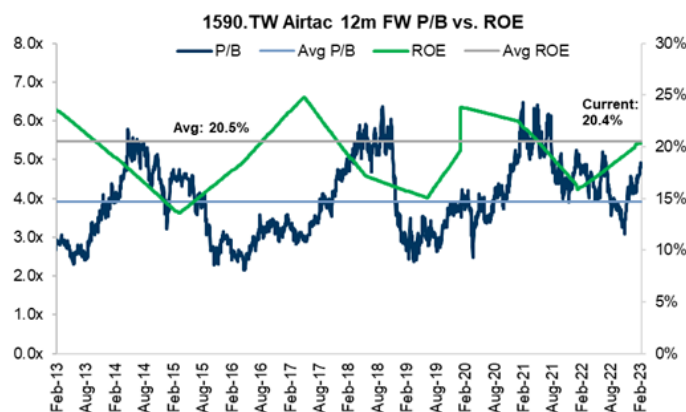
Maintain Buy (on CL) with a new 12-m TP of NT\$1,400, based on a new 30x 2Q23-1Q24E P/E (from 28x 2023E P/E; 1.1 s.d. higher than 10-year average of 22.6x) and factor in our earnings revisions. Key risks include: (1) rising competition from peers; (2) sharper-than-expected RMB depreciation; and (3) a worsening of the COVID situation.

**Exhibit 12: AirTAC's past 10-year PE band (1-year forward)**

Source: Company data, Goldman Sachs Global Investment Research

**Exhibit 13: AirTAC's past 10-year PB band (1-year forward) - the stock price is trading slightly above past 10-year average**

Source: Company data, Goldman Sachs Global Investment Research

**Exhibit 14: AirTAC's PB multiple could continue to go up with improving ROE**


Source: Company data, Goldman Sachs Global Investment Research

**Exhibit 15: P&L summary**

NT\$m	1Q22	2Q22	3Q22	4Q22	1Q23E	2Q23E	3Q23E	4Q23E	1Q24E	2Q24E	3Q24E	4Q24E	2021	2022	2023E	2024E	2025E
Revenue	6,509	7,222	6,078	6,265	5,975	7,967	8,697	8,700	8,275	9,529	9,617	9,675	25,400	26,074	31,339	37,096	40,187
Gross profit	2,808	3,366	2,814	2,905	2,750	3,841	4,272	4,271	4,039	4,667	4,749	4,789	12,337	11,893	15,133	18,245	19,987
Operating expense	(997)	(1,174)	(1,110)	(1,069)	(1,064)	(1,163)	(1,322)	(1,349)	(1,272)	(1,277)	(1,327)	(1,363)	(4,121)	(4,350)	(4,898)	(5,239)	(5,546)
Operating income	1,811	2,192	1,704	1,836	1,686	2,677	2,950	2,922	2,766	3,390	3,422	3,426	8,216	7,543	10,235	13,005	14,441
Pretax income	2,191	2,072	1,802	1,759	1,686	2,829	3,080	3,213	2,867	3,445	3,478	3,610	8,385	7,824	10,808	13,401	14,941
Taxes expense	(513)	(470)	(411)	(417)	(411)	(690)	(708)	(691)	(674)	(792)	(802)	(870)	(1,943)	(1,811)	(2,501)	(3,138)	(3,511)
Net income	1,678	1,602	1,391	1,342	1,275	2,139	2,372	2,522	2,194	2,653	2,676	2,740	6,442	6,013	8,307	10,263	11,430
EPS, NT\$	8.39	8.01	6.96	6.71	6.37	10.70	11.86	12.61	10.97	13.26	13.38	13.70	33.38	30.07	41.54	51.32	57.15
<b>Ratio analysis and assumption</b>																	
<b>As % of sales</b>																	
Gross margin	43.1%	46.6%	46.3%	46.4%	46.0%	48.2%	49.1%	49.1%	48.8%	49.0%	49.4%	49.5%	48.6%	45.6%	48.3%	49.2%	49.7%
Operating expense ratio	15.3%	16.3%	18.3%	17.1%	17.8%	14.6%	15.2%	15.5%	15.4%	13.4%	13.8%	14.1%	16.2%	16.7%	15.6%	14.1%	13.8%
Operating margin	27.8%	30.4%	28.0%	29.3%	28.2%	33.6%	33.9%	33.6%	33.4%	35.6%	35.6%	35.4%	32.3%	28.9%	32.7%	35.1%	35.9%
Net margin	25.8%	22.2%	22.9%	21.4%	21.3%	26.8%	27.3%	29.0%	26.5%	27.8%	27.8%	28.3%	25.4%	23.1%	26.5%	27.7%	28.4%
<b>QoQ growth (%)</b>																	
Revenue	13%	11%	-16%	3%	-5%	33%	9%	0%	-5%	15%	1%	1%					
Gross profit	3%	20%	-16%	3%	-5%	40%	11%	0%	-5%	16%	2%	1%					
Operating income	1%	21%	-22%	8%	-8%	59%	10%	-1%	-5%	23%	1%	0%					
Net income	5%	-5%	-13%	-4%	-5%	68%	11%	6%	-13%	21%	1%	2%					
<b>YoY growth (%)</b>																	
Revenue	10%	3%	-9%	9%	-8%	10%	43%	39%	38%	20%	11%	11%	33%	3%	20%	18%	8%
Gross profit	-2%	-3%	-14%	7%	-2%	14%	52%	47%	47%	22%	11%	12%	31%	-4%	27%	21%	10%
OPEX	11%	12%	-11%	16%	7%	-1%	19%	26%	20%	10%	0%	1%	18%	6%	13%	7%	6%
Operating income	-8%	-9%	-16%	2%	-7%	22%	73%	59%	64%	27%	16%	17%	38%	-8%	36%	27%	11%
Net income	16%	-10%	-13%	-16%	-24%	34%	70%	88%	72%	24%	13%	9%	33%	-7%	38%	24%	11%

Source: Company data, Goldman Sachs Global Investment Research

## Investment Thesis, Price Target Risks and Methodology

AirTAC is a global manufacturer of pneumatic components such as pneumatic control components, actuators, F.R.L. combinations, accessories. AirTAC also offers after-sales support on its products, including installation, application and maintenance. We continue to see AirTAC as one of our top picks in the Taiwan Automation sector and believe it is attractively positioned given: (1) Its potential for earnings expansion backed by its solid execution with ongoing share gains and rising linear guide contribution. (2) Its attractive pricing, solid technology skillset, and strong service infrastructure. (3) EV/EV battery, automotive and electronics are the three key segments for AirTAC to grow. The company believes EV/EV battery industry demand will keep expanding, supported by the Chinese government, and they believe they can continue to gain share in the automotive market in China. We expect the company should see better revenue/profitability in the long term given their share gainer position in the China pneumatic market and positive outlook in the linear guide market, which should lead to a higher P/E multiple in the long term compared with its recent trading range (one-year



forward P/E is well below our target multiple), and thus justifies our Buy rating (on CL) for AirTAC.

Our 12m TP of NT\$1,400 is based on 30x 2Q23-1Q24E P/E (1.1x s.d. higher than the past 10-year average of 22.6x). Key risks include: (1) rising competition from peers; (2) sharper-than-expected Rmb depreciation; and (3) a worsening of the COVID situation.

<b>1590.TW</b>	12m Price Target: <b>NT\$1,400.00</b>	Price: <b>NT\$1,095.00</b>	Upside: <b>27.9%</b>
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Buy <b>CL</b>		GS Forecast			
Market cap: NT\$209.4bn / \$7.0bn Enterprise value: NT\$209.7bn / \$7.0bn 3m ADTV: NT\$649.2mn / \$21.2mn Taiwan Taiwan Industrials M&A Rank: 3 Leases incl. in net debt & EV?: No Asia ex. Japan Conviction List	<b>Revenue (NT\$ mn) New</b>	<b>12/22</b>	<b>12/23E</b>	<b>12/24E</b>	<b>12/25E</b>
		<b>26,074.0</b>	<b>31,338.8</b>	<b>37,095.6</b>	<b>40,187.4</b>
	Revenue (NT\$ mn) Old	26,088.5	30,668.8	35,312.9	39,048.6
	EBITDA (NT\$ mn)	9,296.4	12,146.0	14,965.7	16,551.7
	<b>EPS (NT\$) New</b>	<b>30.07</b>	<b>41.54</b>	<b>51.32</b>	<b>57.15</b>
	EPS (NT\$) Old	29.25	39.50	47.59	53.71
	P/E (X)	29.2	26.4	21.3	19.2
	P/B (X)	4.5	5.0	4.4	3.9
	Dividend yield (%)	1.4	1.5	2.1	2.3
	CROCI (%)	17.7	21.6	24.1	25.0
		<b>12/22</b>	<b>3/23E</b>	<b>6/23E</b>	<b>9/23E</b>
	EPS (NT\$)	6.71	6.37	10.70	11.86

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 8 Feb 2023 close.

# Disclosure Appendix

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**Growth** is based on a stock's forward-looking sales growth, EBITDA growth and EPS growth (for financial stocks, only EPS and sales growth), with a higher percentile indicating a higher growth company. **Financial Returns** is based on a stock's forward-looking ROE, ROCE and CROCI (for financial stocks, only ROE), with a higher percentile indicating a company with higher financial returns. **Multiple** is based on a stock's forward-looking P/E, P/B, price/dividend (P/D), EV/EBITDA, EV/FCF and EV/Debt Adjusted Cash Flow (DACF) (for financial stocks, only P/E, P/B and P/D), with a higher percentile indicating a stock trading at a higher multiple. The **Integrated** percentile is calculated as the average of the Growth percentile, Financial Returns percentile and (100% - Multiple percentile).

Financial Returns and Multiple use the Goldman Sachs analyst forecasts at the fiscal year-end at least three quarters in the future. Growth uses inputs for the fiscal year at least seven quarters in the future compared with the year at least three quarters in the future (on a per-share basis for all metrics).

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There are no company-specific disclosures for: Airtac International Group (NT\$1,095.00)

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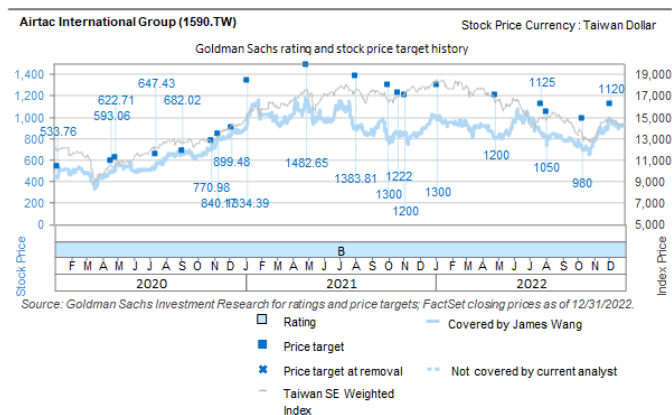
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	Rating Distribution				Investment Banking Relationships		
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Global	47%	37%	16%		64%	58%	48%

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