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Zhejiang Dahua Technology (002236.SZ)

1Q26 beat, a 50% 3-year CAGR target for AI business

CITI'S TAKE

Dahua released its FY25 and 1Q26 financial results and held an investor briefing meeting on 18 April. Key highlights: 1) FY25 Rev/NP in line with prior prelim results while 1Q26 ahead; 2) Revenue related to AI large models reached RMB 878 million in 2025. The company's ESOP outlines a minimum 50% CAGR target for AI segment over the next three years; 3) Incubated innovation units and ToB segments have transitioned into profitable, core revenue contributors. 4) Management expects to utilise proactive inventory management to navigate supply chain and geopolitical risks, and to deliver a stable profit margin. 2Q26 gross margin to remain relatively stable and consistent with 1Q26 levels. For 2H26, margins may face pressure from increases in upstream component prices.

Sell	
Price (17 Apr 26 15:00)	Rmb19.160
Target price	Rmb19.300
Expected share price return	0.7%
Expected dividend yield	2.0%
Expected total return	2.7%
Market Cap	Rmb62,974M
	US$9,237M

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4Q25/1Q26 review: FY25 revenue/NP recorded Rmb32.7bn/3.86bn, up 2% YoY/33% YoY, in line with its prior prelim results. Revenue could be over 5% YoY excluding the disposal of subsidiary impact. This was supported by a 1.78 percentage point YoY rise in gross margin to 40.62%, which the company attributes to a shift toward higher value-added products and cost-control measures. Operating cash flow increased by 44.2% YoY to RMB 3.91 billion, and accounts receivable decreased by 9.2% YoY, reflecting changes in collection cycles. **4Q25** Revenue/NP was up 1%/-11% YoY, GM improved 3.8ppt YoY to 37.4%, 1.5ppt/2.4ppt below CitiE/BBGe. Opex increased by 6% to Rmb3.5bn and OP reached Rmb231mn, but 64% /52% below CitiE/BBGe. **1Q26** revenue/NP grew 10%/7% YoY to Rmb6.9bn/698mn, due to unconsolidated its thermal imaging business Huacheng. Excluding Huacheng, revenue could grow by 19.35% YoY, net profit excluding non-recurring gains and losses rose by over 20% YoY. These figures adjust the impact of an RMB 237 million foreign exchange loss during 1Q26, compared to an RMB 92 million FX gain in 1Q25. GM improved 3.6ppt YoY to 43%, 1.8ppt/0ppt ahead CitiE/BBGe.

Figure 1. 4Q25 results summary

	4Q25			3Q25		4Q24		Consensus	
Rmb m	Reported	Citi Est.	Diff%	Actual	QoQ	Actual	YoY	BBG	Diff%
Revenue	9,831	10,060	-2.3%	7,731	27.2%	9,731	1.0%	10,437	-5.8%
Gross profit	3,680	3,913	-5.9%	3,156	16.6%	3,276	12.4%	4,155	-11.4%
OPEX	(3,449)	(2,593)	33.0%	(2,593)	33.0%	(3,248)	6.2%	(3,674)	-6.1%
Operating profit	231	635	-63.6%	564	-59.0%	28	739.7%	481	-52.0%
Pre-tax profit	378	766	-50.6%	1,115	-66.1%	415	-8.8%	646	-41.5%
Net profit	322	643	-49.8%	1,060	-69.6%	361	-10.6%	435	-25.8%
Ratio									
Gross margin	37.4%	38.9%	-1.5ppts	40.8%	-3.4ppts	33.7%	3.8ppts	39.8%	-2.4ppts
OPEX to Sales ratio	35.1%	25.8%	9.3ppts	33.5%	1.6ppts	33.4%	1.7ppts	35.2%	-0.1ppts
Operating margin	2.4%	6.3%	-4.0ppts	7.3%	-4.9ppts	0.3%	2.1ppts	4.6%	-2.3ppts
Net margin	3.3%	6.4%	-3.1ppts	13.7%	-10.4ppts	3.7%	-0.4ppts	4.2%	-0.9ppts

Source: Citi Research, Bloomberg, Company Reports

Figure 2. 1Q26 results summary

	1Q26			4Q25		1Q25		Consensus	
Rmb m	Reported	Citi Est.	Diff%	Actual	QoQ	Actual	YoY	BBG	Diff%
Revenue	6,902	6,567	5.1%	9,831	-29.8%	6,256	10.3%	7,911	-12.8%
Gross profit	2,967	2,706	9.6%	3,680	-19.4%	2,462	20.5%	3,403	-12.8%
OPEX	(2,295)	(2,593)	-11.5%	(3,449)	-33.5%	(2,239)	2.5%	n.a.	n.a.
Operating profit	672	357	88.4%	231	190.7%	223	200.6%	n.a.	n.a.
Pre-tax profit	766	725	5.6%	378	102.5%	697	9.8%	1,237	-38.1%
Net profit	698	623	12.0%	322	116.4%	653	6.8%	494	41.2%
Ratio									
Gross margin	43.0%	41.2%	1.8ppts	37.4%	5.5ppts	39.4%	3.6ppts	43.0%	0.0ppts
OPEX to Sales ratio	33.3%	39.5%	-6.2ppts	35.1%	-1.8ppts	35.8%	-2.5ppts	n.a.	n.a.
Operating margin	9.7%	5.4%	4.3ppts	2.4%	7.4ppts	3.6%	6.2ppts	n.a.	n.a.
Net margin	10.1%	9.5%	0.6ppts	3.3%	6.8ppts	10.4%	-0.3ppts	6.2%	3.9ppts

Source: Citi Research, Bloomberg, Company Reports

Key takeaways from results briefing

AI transformation facilitates commercialisation

AI remains a primary focus of Dahua's long-term strategy, with a dual focus on external commercialization and internal efficiency. Externally, the company is developing end-to-end AI capabilities that include intelligent perception, vertical large models, and scenario applications. Revenue related to AI large models reached RMB 878 million in 2025. The company's ESOP outlines a minimum 50% CAGR target for AI segment over the next three years, aiming to increase penetration across the public security, transportation, and energy sectors.

Internally, Dahua has implemented an AI enablement program with targets to have 35% of code generated by AI and 60% of project processes integrated with AI nodes by the end of 2026. The company estimates this initiative could improve R&D efficiency by 20-30% with an incremental cost of approximately RMB 2,000 per capita annually.

Diversified business resilience and disciplined risk management

Dahua's diversified business segments showed strong growth momentum. The domestic ToB (business-to-business) segment saw revenue increase by 11.38% YoY in FY25, supported by developments in semiconductors, energy storage, and manufacturing. The ToG (business-to-government) segment is positioned to potentially be influenced by digital infrastructure spending under the 15th Five-Year Plan. The distribution business, which underwent restructuring, reported a turnaround in 2H25. Overseas business revenue was RMB 15.99 billion for FY25, with growth observed in Europe, Oceania, and Africa, alongside steady order volume in 1Q26.

Stable margin via proactive supply chain management

Management anticipates the 2Q26 gross margin to remain relatively stable and consistent with 1Q26 levels. For 2H26, margins may face pressure from increases in upstream component prices. To manage these supply chain factors, the company is utilizing weekly inventory reviews, advance stocking, research into lower-cost alternatives, and pricing adjustments. The stated goal is to balance cost pass-through with demand stability to maintain steady gross profit volume.

Zhejiang Dahua Technology

Valuation

We set our target price for Dahua at Rmb19.3 based on 16.9x NTM PE (0.5SD above 10-year average).

Risks

Upside risks that could prevent Dahua shares from reaching our target price include: (1) lower operating expenses to lift profit; (2) successful expansion into overseas markets; (3) better-than expected growth of the surveillance market; and (4) breakthrough in developing surveillance solutions.