

25 July 2014

Brilliance China (1114.HK)

Accelerated segmentation product strategy

Hong Kong | AUTOMOBILE | COMPANY UPDATES

Rating: **Accumulate**

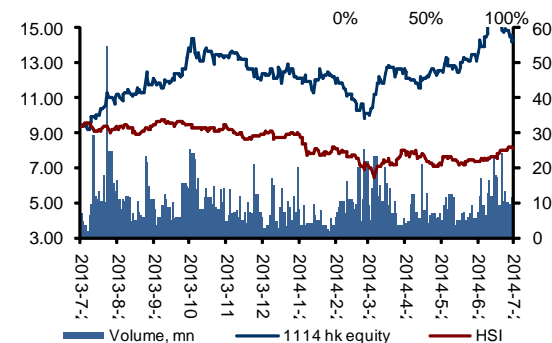
Maintain Accumulate

Target Price (HKD)	16.45
Forecast Dividend (HKD)	0.25
Closing Price (HKD)	14.32
Potential Return	15.7%

Company Description

Brilliance mainly engaged in manufacturing and selling light trucks and components, the main products is Jinbei Haise, with the largest shares consistently, and high-end saloon car BMW 3&5 series, SUV X1 from BMW Brilliance Automobile(BBA), its 50%-50% JV, which is the main source of the Group's profits.

Raw Beta (Past 2yrs weekly data)	1.08
Market Cap. (HKD bn)	71,969
Enterprise Value (HKD mn)	58,394
52 week range (HKD)	8.98 - 16.14
Closing Price in 52 week range	



Major Shareholders

1. Huachen Automotive Group Holdings	42.48%
2. Templeton Asset Management Ltd	18.02%

Valuation Method

P/E

Analyst

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- Strong growth for BBA 1H2014:** Owing to the continuing effect of capacity release, BBA (Brilliance BMW) delivered 140 thousand cars in the first half of 2014, a year-on-year increase of 37%, out of which SUV model X1 increased by 107% year-on-year to 22 thousand, X3 increased by 55% to 46 thousand, and X5 increased by 51% to 71 thousand. The company's sales goal in 2014 is 260 thousand cars, a 30% year-on-year increase, and in half a year it has achieved 53.8% of the sales goal for the year. Since the capacity of Dadong factory for production of series 5 has been approaching its limit, we believe in the coming one-year BBA's sales increase will be mainly contributed by series 3 and X1.
- JV Contract renewal in advance is expected to eliminate uncertainty:** 4 years ahead of the expiration of the joint venture contract, BMW Group and the company have announced recently that joint venture contract would be extended to 2028; this move is expected to eliminate the uncertainty of the source for future profitability, and is conducive to the introduction of new BMW models and their technologies, which is beneficial to the company's stock performance and the level of valuation.
- Accelerated segmentation product strategy:** BMW Group has issued the guidance on the future planning of Chinese market, including: 3 new models will realize localized production in China; Continue to increase the total capacity of BBA's Dadong factory and Tiexi factory in Shenyang; BMW's 3-cylinder and 4-cylinder gasoline engines are going to be put into production in China in 2016. It is learned that the 3 new models for domestic production in future are respectively BMW 2X Active Tourer van, BMW X3 and one new entry-level model lower than the level of X3, which will increase the vehicle types of domestic production in China from currently 3 models to 6 models. For SUV model X3, the wheelbase will be extended, which is more likely to meet the vehicle purchase needs of domestic consumers at present, and the future performance is worthy of expectation. After the completion of BBA's new engine plant, production of advanced 3-cylinder and 4-cylinder gasoline engines will be officially started in 2016, which will positively improve the capacity and quality of BBA.

Key Financial Summary

FYE	12/13	12/14F	12/15F	12/16F
Revenue (RMB mn)	6103	6229	6495	6989
Net Profit, adj. (RMB mn)	3374	4319	5867	7599
EPS, adj. (RMB)	0.67	0.86	1.17	1.51
P/E (X),adj.	16.8	13.1	9.6	7.4
BVPS (RMB)	2.59	3.29	4.44	5.41
P/B (X)	4.3	3.4	2.5	2.1
DPS (RMB)	0.08	0.10	0.13	0.17
Div. Yield (%)	0.7%	0.9%	1.2%	1.5%

Source: Bloomberg, PSR est.

*All multiples & yields based on current market price

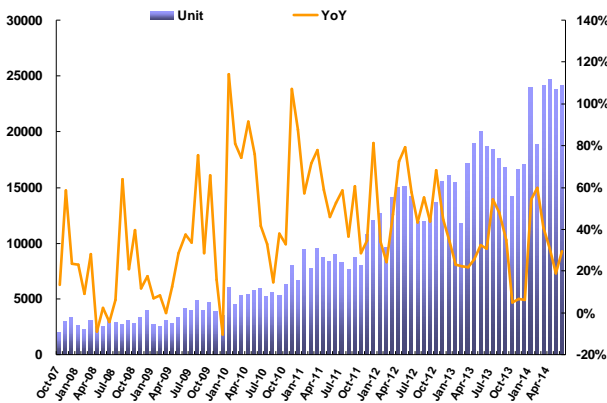
How we view this

We believe that, after experiencing the explosive growth in past few years, the increase rate of China's luxury car market begins to slow down, with structure-based and pluralism market development trend becoming apparent, so BMW's accelerated introduction of segmentation products is conducive to continuous development of new segment markets.

Investment Action

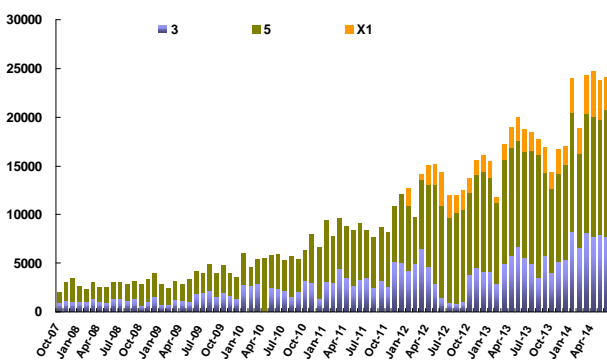
According to above, we revised our target price to HK\$16.45, based on 15/11/8.5xP/E in 2014/2015/2016, which we believe is rational considering its high ROE and fast growth ahead among peers, and the suggestions of "accumulate" rating be given.

Fig 1. BBA's monthly sales (units)



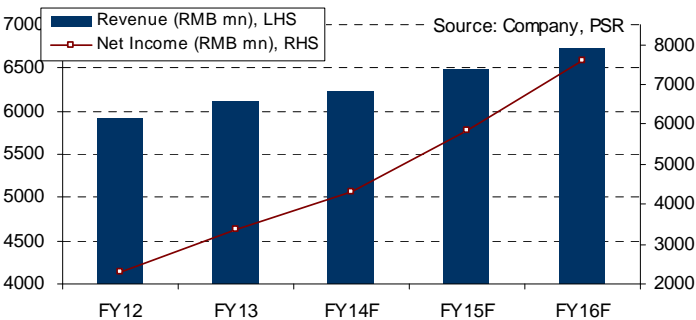
Source: Company, PSR

Fig 2. BBA's monthly sales by models (units)



Source: Company, PSR

Fig 5. View of BC's top line and bottom line in IS



Source: Company, PSR

Fig 3. BMW's SUV X3



Source: Company, PSR

Fig 4. BMW's 2 series Active Tourer



Source: Company, PSR

Fig 6. Peer's comparison

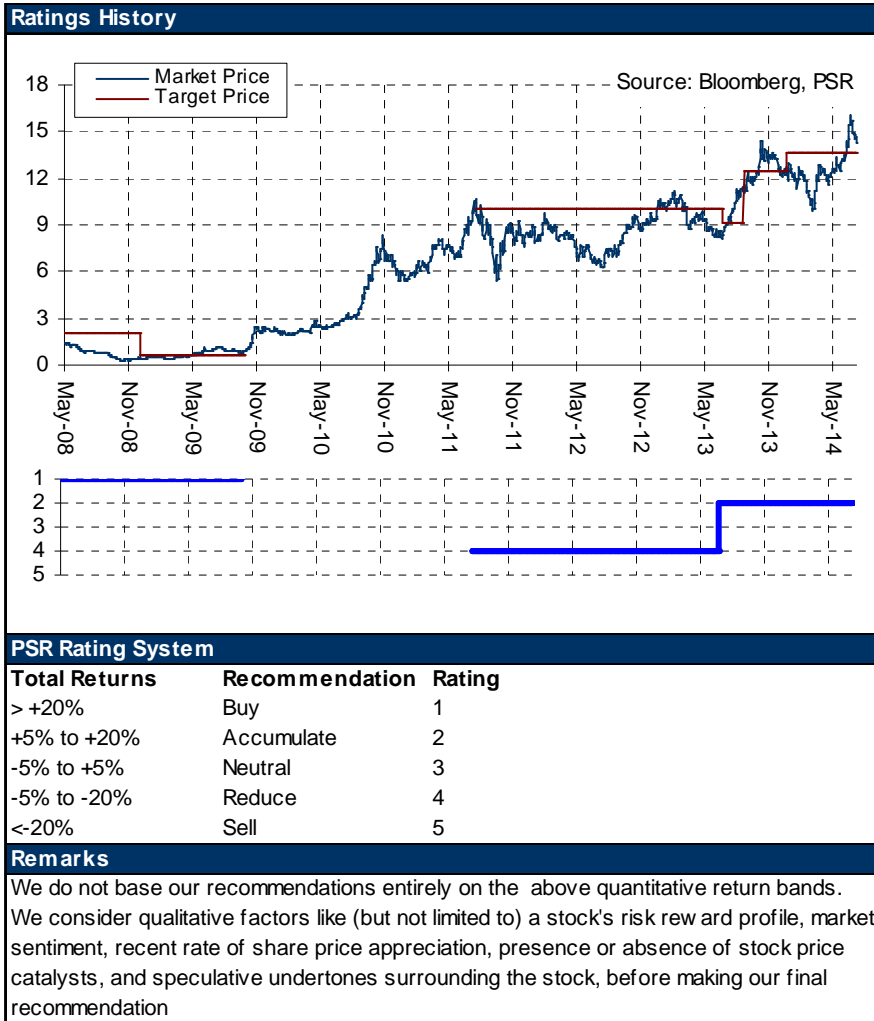
Ticker	Name	Mark	Best		Best		Best		ROA	
		Cap	Best	P/B	Best	P/E	EV/BE	P/B	LF	ROE
		USD-mil	P/B	(Y+1)	P/E	(Y+1)	st	P/B	(%)	(%)
2238 HK Equity	GAC	8054	1.4	1.2	11.9	9.2	127.9	1.5	4.9	8.2
1211 HK Equity	BYD	17634	3.5	3.3	73.2	48.8	21.7	4.0	0.7	2.6
489 HK Equity	DONGFENG	16231	1.4	1.2	8.6	7.6	88.3	1.6	11.8	18.0
2333 HK Equity	GWM	12810	2.1	1.7	7.9	6.5	6.1	2.6	17.3	33.2
1114 HK Equity	BRILLIANCE	10207	3.8	2.9	14.6	12.2	N/A	4.9	19.3	29.3
175 HK Equity	GEELY	3327	1.1	0.9	7.9	6.6	4.0	1.3	8.2	18.4
F US Equity	FORD	68488	2.3	1.9	13.1	9.1	6.1	2.6	3.2	29.4
GM US Equity	GM	60043	1.4	1.3	12.3	8.0	3.7	1.5	2.7	8.9
RNO FP Equity	RENAULT	28421	0.8	0.8	9.5	7.2	9.5	0.9	0.8	2.5
UG FP Equity	PEUGEOT	11964	0.9	0.8	N/A	12.1	11.1	0.7	-3.7	-28.3
VOW GR Equity	VW	933217	0.9	0.9	8.4	7.5	7.1	1.0	2.9	11.0
BMW GR Equity	BMW	632044	1.6	1.4	10.7	10.2	9.5	1.7	3.9	16.1
DDAIF US Equity	DAIMLER	797733	1.5	1.4	11.9	10.2	9.9	1.7	4.1	17.0
TTMT IN Equity	TATA	153634	2.5	1.9	8.8	7.6	4.2	3.4	6.3	28.1
7203 JP Equity	TOYOTA	1466094	1.3	1.2	9.4	8.8	10.0	1.3	5.1	8.5
7267 JP Equity	HONDA	473256	1.1	1.0	10.6	8.8	8.9	1.1	3.4	7.8
7201 JP Equity	NISSAN	318603	0.9	0.9	10.6	8.9	10.7	0.9	2.9	9.9
7269 JP Equity	SUZUKI	117221	1.2	1.1	14.0	13.0	4.3	1.2	4.5	7.5
7261 JP Equity	MAZDA	104332	2.2	1.8	11.6	8.0	7.3	2.3	4.3	7.1
7211 JP Equity	MITSUBISHI	81152	1.9	1.7	10.3	9.4	7.1	12.4	7.8	N/A
005380 KS Equity	HYUNDAI	48798	1.0	N/A	N/A	N/A	N/A	1.1	6.5	10.5
000270 KS Equity	KIA	21688	0.9	N/A	6.0	5.8	N/A	1.2	10.9	15.6

Source: Bloomberg, PSR

FYE DEC	FY12	FY13	FY14F	FY15F	FY16F
Valuation Ratios					
P/E (X), adj.	25.1	16.8	13.1	9.6	7.4
P/B (X)	5.8	4.3	3.4	2.5	2.1
Dividend payout Yield (%)	0.0%	11.7%	11.2%	11.2%	11.3%
Dividend Yield (%)	0.0%	0.7%	0.9%	1.2%	1.5%
Per share data (RMB)					
EPS, (Basic)	0.458	0.671	0.859	1.167	1.512
EPS, (Diluted)	0.456	0.669	0.856	1.163	1.506
DPS	0.00	0.08	0.10	0.13	0.17
BVPS	1.99	2.59	3.29	4.44	5.41
Growth & Margins (%)					
Growth					
Revenue	-8.2%	3.2%	2.1%	4.3%	7.6%
EBIT	15.9%	42.7%	46.3%	31.2%	28.7%
Net Income, adj.	27.0%	46.6%	28.0%	35.9%	29.5%
Margins					
Gross margin	11.8%	11.2%	10.7%	10.5%	10.5%
EBIT margin	40.5%	56.0%	80.3%	101.0%	120.8%
Net Profit Margin	38.9%	55.3%	69.3%	90.3%	108.7%
Key ratios (%)					
ROE	27.1%	29.3%	29.2%	30.2%	30.7%
ROA	15.9%	19.3%	20.7%	22.9%	24.6%

Income Statement (RMB mn)					
Revenue	5916	6103	6229	6495	6989
Gross profit	696	687	666	682	734
EBIT	2395	3416	4999	6559	8439
Profit before tax	2295	3325	4875	6431	8328
Tax	-58	-8	-390	-444	-575
Profit for the period	2237	3316	4485	5987	7754
Minority interests	-64	-58	166	120	155
Total capital share	5024	5026	5026	5026	5026
Net profit	2301	3374	4319	5867	7599

Source: PSR



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Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within \pm 5% from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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