

28 October 2014

# Geely Automobile (175.HK)

## Cold export, warmer domestic

### HONG KONG | AUTOMOBILE | COMPANY UPDATES

- September saw 39019 sales units, down by 9% YoY, which sharply narrowed from the double-digit decline rate before, but up by 41% MoM.
- Seen from the MoM sales, the sales of New Emgrand and SUV have contributed to nearly 70% of the incremental sales.
- The Company had a total sales volume of 86819 cars in the third quarter, which was 22.7% less than that of last year's same period.
- The sales volume of the first three quarters totalled 274005 cars with YoY decline rate of 27%, which achieved 64% of its annual goal. It means that in order to reach the goal successfully, the average monthly sales volume have to reach as high as 52000 cars for the remaining three months of this year.
- Export sales reported 4677 cars in September, down by 45% YoY, still had a big distance to the average monthly sales of 10000 in last year.
- The domestic sales volume had clearly rebounded and the YoY decline rate downed to 1%, while the MoM rate had a significant rebound of 48%.
- In Sep., Geely signed a letter of intent for cooperation with Corun, a leader in the Ni-MH battery technology field in China, and planned to set up a JV.

#### How we view this

Through adjustment over most of this year, Geely has shown an increasingly clear brand strategy. The government finally launched a new national policy in September this year, which obviously indicated the intention to support self-owned brands. Geely has 6 car models that were included, accounting for more than 60% of the last year's total sales volume of the company. The restart of the new national policies will help the sales volume of the company to speed up again.

As the models co-produced by Geely and Volvo has to wait until after 2016, the result of Geely in recent 2 years would be constrained by the limitation of popular models; the future sales volume of its new energy vehicles is also subjected to the promotion and development of the domestic new energy vehicles market. However, the acceleration of the new energy vehicle commercialization will stimulate the market expectation and the level of its valuation.

#### Investment Action

From our unrevised financial forecast, we lift our target price to HK\$4.00, based on 12.6/10.5xP/E in 2014/2015, and the suggestions of "Buy" rating be given.

#### Key Financial Summary

FYE	12/12	12/13	12/14F	12/15F
Revenue (RMB mn)	24,628	28,708	23,115	26,717
Net Profit, adj. (RMB mn)	2,040	2,663	2,205	2,629
EPS, adj. (RMB)	0.27	0.32	0.25	0.30
P/E (X), adj.	9.9	8.2	10.5	8.8
BVPS (RMB)	1.59	1.93	1.99	2.30
P/B (X)	1.7	1.4	1.3	1.1
DPS (RMB)	0.03	0.04	0.03	0.04
Div. Yield (%)	1.2%	1.6%	1.1%	1.4%

Source: Bloomberg, PSR est.

\*All multiples & yields based on current market price

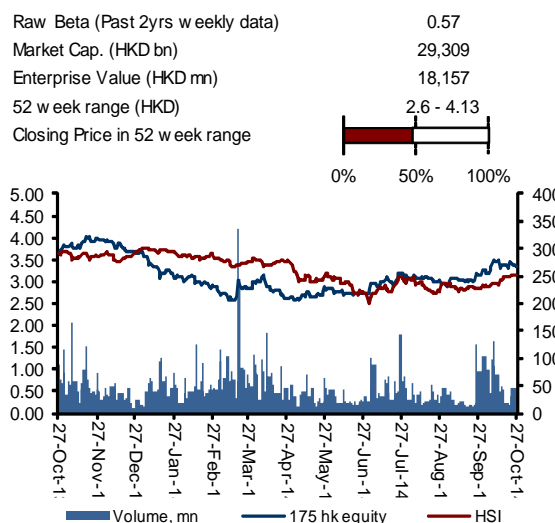
Rating: **Buy**

Upgraded to Buy

<b>Target Price (HKD)</b>	<b>4.00</b>
Forecast Dividend (HKD)	0.04
Closing Price (HKD)	3.33
<b>Potential Return</b>	<b>21.3%</b>

#### Company Description

Geely is one of big-4 Chinese local brand car producers, with manufacture bases in Linhai, Ningbo and Luqiao, Shanghai, Lanzhou, Xiangtan, Jinan Chengdu, and a R&D center. It has more than 10 car models on sale and 625000 units of capacity.



#### Major Shareholders

1. Proper Glory Holding Inc.	27.98%
2. Zhejiang Geely Automobile Company Limited	8.82%
3. JPMorgan Chase & Co.	8.80%

#### Valuation Method

PE

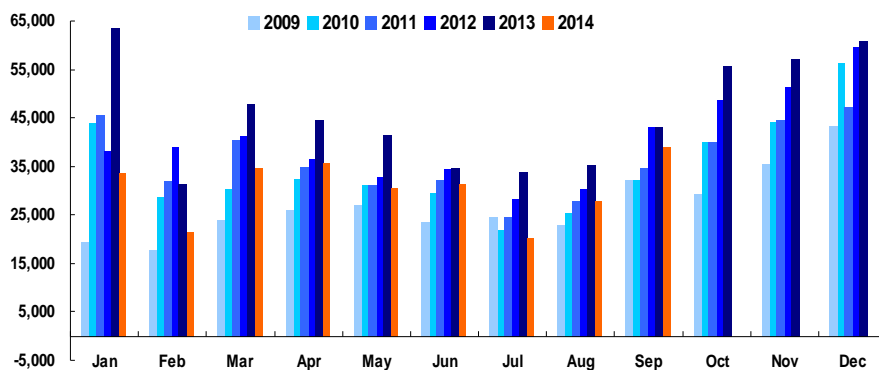
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**The YoY decline rate of sales volume in September narrowed down, while its MoM rate rebounded significantly**

In September, the sales of Geely had a record of 39019 cars with a YoY decline rate of 9%, which sharply narrowed from the double-digit decline rate before. As for the MoM growth rate, it had a significant rebound of 41% compared with the previous month. The New Emgrand launched in the end of July performs strongly and is the main driving force, whose sales in September reached 13794 cars with MoM growth rate of 92%. Moreover, SUV cars showed the tendency of bottoming out, the total sales of which in September were 5766 cars, and remained the same YoY, while rose by 26% MOM. Seen from the MoM sales, both the above have contributed to nearly 70% of the incremental sales.

**Fig 1. Geely monthly sales (units)**

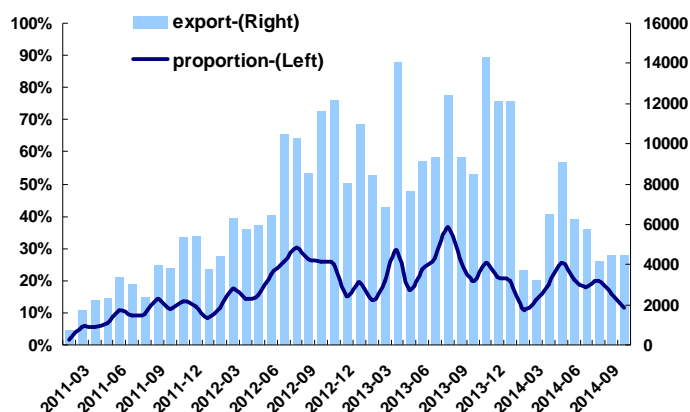


Source: Company, PSR

**The export remains in the downturn, while domestic sales show signs of getting warmer**

Affected by the unstable political situation of the main export market, Geely had an export sales volume of 4677 cars in September. The YoY decline rate was 45%, while MoM rate increased slightly by 5%. It still had a big distance to the average monthly sales of last year, which were 10000 cars. The domestic sales volume had clearly rebounded and the YoY decline rate downed to 1%, while the MoM rate had a significant rebound of 48%.

**Fig 2. Geely monthly exports (units, %)**



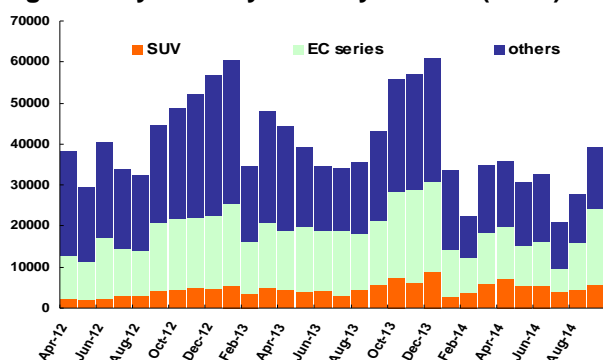
Source: Company, PSR

The Company had a total sales volume of 86819 cars in the third quarter, which was 22.7% less than that of last year's same period. The sales volume of the first three quarters totalled 274005 cars with YoY decline rate of 27%, which achieved 64% of its annual goal. It means that in order to reach the goal successfully, the average monthly sales volume have to reach as high as 52000 cars for the remaining three months of this year.

**Brand adjustment is getting clear day by day, and reapplying the new round of national policies helps speed up the sales of the Company**

Through adjustment over most of this year, Geely has shown an increasingly clear brand strategy: after cancelling three sub-brands and integrating them into one Geely brand, the products of the company will be mainly classified into five product lines in the future, namely KC Series, Emgrand Series, Vision Series, Kingkong Series and Panda Series, while the subsequent integration of dealer channels is expected to be completed within 1 to 2 years.

**Fig 3. Geely monthly sales by models (units)**



Source: Company, PSR

**Fig 4. Geely's new logo**



Source: Company, PSR

The state subsidies for saving energy and benefiting people aiming at small emission economical cars has expired since last year October, while new policies delaying being published restrain the consumer demand on part of low-end cars, especially those self-owned brands, facing the challenge that joint-venture automobile enterprises have launched more competitive low-end car models successively, and the market share of self-owned brands has declined for 12 consecutive months. The government finally launched a new national policy in September this year, which obviously indicated the intention to support self-owned brands. Geely has 6 car models that were included, accounting for more than 60% of the last year's total sales volume of the company. The restart of the new national policies will help the sales volume of the company to speed up again.

**HEV technology commercialization stepping into a fast development period**

During the Beijing Auto Expo in 2014 April, Geely launched the deep HEV model of Emgrand EC7 and the plug-in HEV model of Emgrand Cross, which is expected to be launched at the end of this year and 2015H2 respectively. In September of this year, Geely signed a letter of intent for cooperation with Corun, a leader in the Ni-MH battery technology field in China, and planned to set up a joint venture company. Geely would contribute assets like HEV powertrain system CHS, etc., while Corun would contribute assets like automobile power battery management system BPS, etc. This joint venture company might break the patent block of Toyota's THS technology. With ability to compete with the international HEV giants, its subsequent extensible space is expansive. In addition, the joint venture company may attract more automobile manufacturers to buy the shares in

order to promote technology platformization and mass production, thus to lower the production cost and improve product competitiveness.

**Fig 5. Emgrand Cross PHEV and HEV EC7**



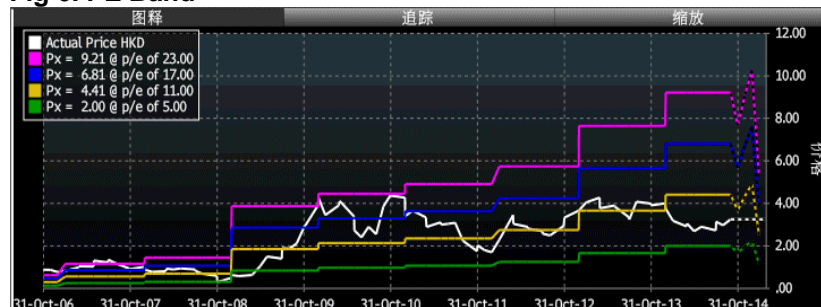
Source: Internet, PSR

### Valuation and Rating

As the models co-produced by Geely and Volvo has to wait until after 2016, the performance of Geely in recent 2 years would be constrained by the limitation of popular models; the future sales volume of its new energy vehicles is also subjected to the promotion and development of the domestic new energy vehicles market. However, the acceleration of the new energy vehicle commercialization will stimulate the market expectation and the level of its valuation.

From our unrevised financial forecast, we lift our target price to HK\$4.00, based on 12.6/10.5xP/E in 2014/2015, and the suggestions of “Buy” rating be given.

**Fig 6. PE Band**



Source: Bloomberg, PSR

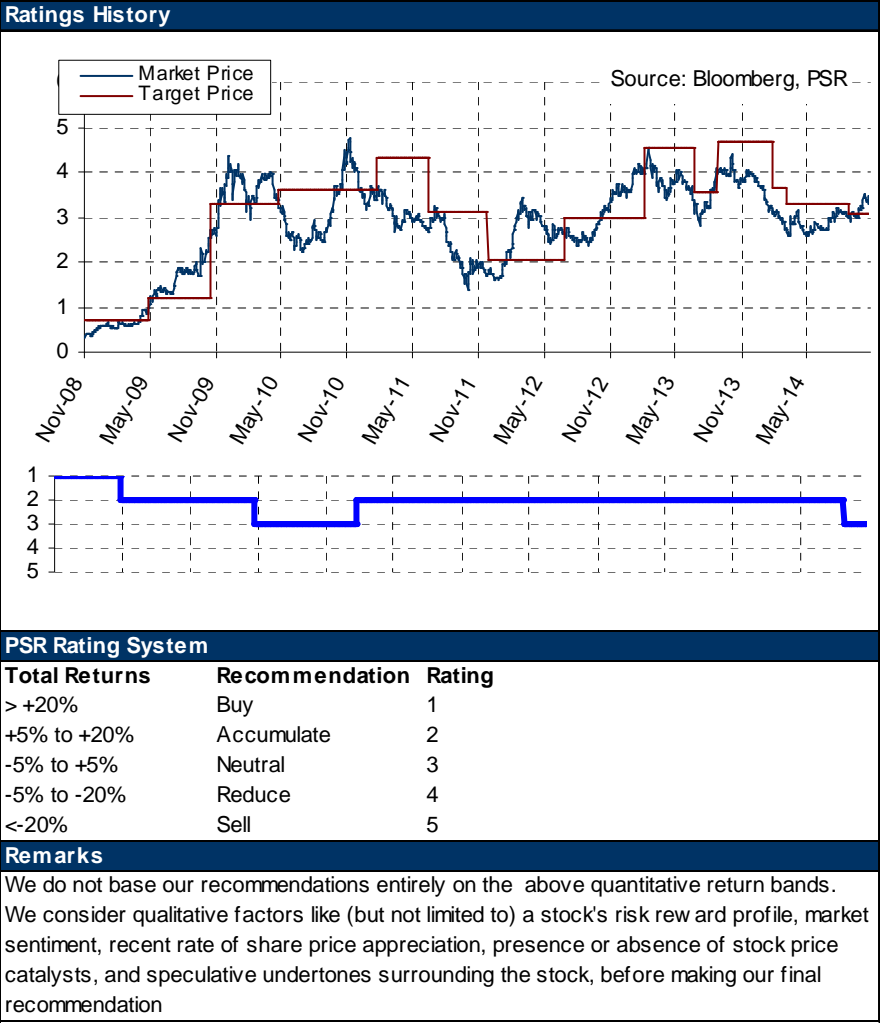
Fig 7. Peer's comparison

Ticker	Name	Cap (USD mil)	Est P/B	Est P/B (Y+1)	Est P/E	Est P/E (Y+1)	EV/BEst EBITDA	P/B	ROA LF (%)	ROE (%)
VOW GR	VW	97908	0.8	0.8	7.6	6.9	7.1	0.9	3.0	11.5
BMW GR	BMW	67585	1.4	1.3	9.3	8.9	9.3	1.5	4.2	17.1
RNO FP	RENAUL	20899	0.6	0.6	8.5	6.1	9.6	0.7	1.7	5.6
UG FP	PSA	9350	0.7	0.7	N/A	10.7	8.9	0.8	-3.0	-21.7
175 HK	GEELY	3812	1.3	1.1	10.1	8.5	5.0	1.4	7.6	15.4
1211 HK	BYD	18226	3.8	3.5	92.9	53.5	20.4	4.0	0.608	2.1
2333 HK	GWM	13694	2.3	1.8	8.7	7.0	7.1	2.5	16.89	30.3
489 HK	Dongfeng	13282	1.1	1.0	6.2	5.7	35.3	1.2	10.87	21.0
200625 CH	CHANGA	10882	2.4	1.7	8.5	6.3	15.4	2.8	10.48	30.4
1114 HK	BRILLIAN	8564	3.1	2.3	10.7	9.3	N/A	3.1	24.46	35.1
2238 HK	GAC	7345	1.0	0.9	9.1	7.1	61.4	1.1	5.7	9.5
TTMT IN	TATA	25254	2.0	1.6	8.8	7.5	4.1	2.5	6.1	23.2
7203 JP	TOYOTA	194344	1.2	1.1	9.5	8.7	9.4	1.3	4.7	13.4
7267 JP	HONDA	55625	1.0	0.9	9.3	8.3	8.1	1.0	4.0	10.6
7201 JP	NISSAN	39490	0.9	0.8	8.7	7.7	8.7	0.9	3.0	10.3
7270 JP	FUJI HEA	24062	2.7	2.2	10.3	9.4	5.0	3.3	12.1	29.2
7269 JP	SUZUKI	17223	1.3	1.2	14.5	13.5	4.6	1.4	4.4	9.3
7261 JP	MAZDA	13009	1.7	1.4	7.7	7.8	5.5	2.0	8.5	29.1
7211 JP	MITSUBI	10366	1.8	1.6	9.2	8.8	4.4	2.1	8.1	N/A
005380 KS	HYUNDA	35914	0.8	N/A	N/A	N/A	N/A	0.8	6.2	10.8
000270 KS	KIA	20843	0.9	N/A	6.1	6.2	N/A	1.2	10.1	16.1
F US	FORD	55850	2.0	1.7	13.2	8.9	5.7	2.1	3.2	28.8
GM US	GM	49695	1.2	1.1	11.7	7.0	3.2	1.2	1.7	7.6
Average		35358	1.6	1.4	13.6	10.3	11.9	1.7	N/A	N/A

Source: Bloomberg, PSR

FYE DEC	FY11	FY12	FY13	FY14F	FY15F
<b>Valuation Ratios</b>					
P/E (X), adj.	13.2	9.9	8.2	10.5	8.8
P/B (X)	2.1	1.7	1.4	1.3	1.1
Dividend Yield (%)	1.0%	1.2%	1.6%	1.1%	1.4%
Dividend payout ratio (%)	14.6%	11.8%	13.9%	12.0%	12.4%
<b>Per share data (RMB)</b>					
EPS, (Basic)	0.207	0.271	0.317	0.251	0.299
EPS, (Diluted)	0.192	0.263	0.303	0.251	0.299
DPS	0.028	0.031	0.042	0.030	0.037
BVPS	1.29	1.59	1.93	1.99	2.30
<b>Growth &amp; Margins (%)</b>					
<b>Growth</b>					
Revenue	4.3%	17.5%	16.6%	-19.5%	15.6%
EBIT	11.6%	13.8%	22.8%	-15.8%	18.9%
Net Income, adj.	12.8%	32.2%	30.5%	-17.2%	19.2%
<b>Margins</b>					
Gross margin	18.2%	18.5%	20.1%	19.5%	19.7%
EBIT margin	11.4%	11.1%	11.6%	12.2%	12.5%
Net Profit Margin	7.4%	8.3%	9.3%	9.5%	9.8%
<b>Key ratios (%)</b>					
ROE	17.5%	18.2%	18.3%	13.2%	14.1%
ROA	5.6%	6.5%	7.9%	6.9%	7.2%
<b>Income Statement (RMB mn)</b>					
Revenue	20,965	24,628	28,708	23,115	26,717
Gross profit	3,820	4,559	5,766	4,503	5,274
EBIT	2,394	2,724	3,344	2,816	3,349
Profit before tax	2,183	2,529	3,304	2,807	3,302
Tax	(467)	(479)	(624)	(590)	(660)
Profit for the period	1,716	2,050	2,680	2,218	2,642
Minority interests	(172)	(10)	(17)	(13)	(13)
Total capital share	7,450	7,466	8,392	8,801	8,801
Net profit	1,543	2,040	2,663	2,205	2,629

Source: PSR





**PHILLIP RESEARCH STOCK SELECTION SYSTEMS**

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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