

Huayu Auto (600741.CH)

Undervalued Industry Leader

China | Automobile parts | Company Initiation

11 August 2015

- With its headquarters in Shanghai, HUAYU Automotive Systems (HASCO) mainly operates in R&D, manufacturing and selling of auto parts, which are the key areas of the auto parts and components business. Its six major business lines include metal forming and dies / molds, interior and exterior trimming parts, electronic and electric parts, functional parts, hot working parts and new energy vehicle parts. The Company was previously under the auto components business of SAIC. It is the key auto components platform of SAIC.

- HASCO is the pioneer of China's auto component industry. It is a listed integrated auto parts and components supplier, with the largest production capacity, the most comprehensive product offering, the broadest customer coverage and the strongest R&D capability in China. Many of its joint ventures companies, which are set up by SAIC with the world's leading auto parts and components players, are the leaders in their respective sub-segments. As of the end of 2014, the subsidiaries and related companies of HASCO have established 261 R&D, manufacturing and service bases in China. 14 manufacturing bases have also been set up in various overseas countries, such as USA, Germany, Thailand, Russia, Australia, Czech and India. As its businesses sprawl across broad segments that cover both the Chinese and overseas market, it starts to enjoy the benefits of clustering effects.

- As for breakdown of profit by business lines, functional parts and interior & exterior trimming parts are the two largest profit contributors, accounting for 43% and 36% of total profits. Electronic and electric parts rank the third with 10% of profit contribution. Metal forming and dies / molds and hot working parts account for a total of 10% profit. As for the breakdown of profit contribution by invested companies, Yanfeng Visteon Automotive Trim Systems is the major profit centre, contributing to over 70% of HASCO's sales revenue and 47% of net profit.

- HASCO has set up a clear strategy of 'Zero level, neutral, Global'. It has gradually identified and prioritized foci of its future development, namely: the company will continue grow its core businesses through a combination of outward expansion and organic growth, so that it can foster transformation and upgrade of these business lines to support sustainable growth. The completion of acquiring 50% stake in Yanfeng Visteon Automotive Trim Systems in 2013 signaled that the company has entered into a 'Post-JV' strategic transformation. We believe that to attract customers, auto manufacturers will tend to apply more high-end and high-technology auto parts and components in their automobiles. This trend will certainly benefit top-tier auto parts manufacturers such as HASCO.

Investment Thesis

As analyzed above, we revised EPS expectation of the Company to RMB 1.97 and 2.32 of 2015/2016. And we accordingly gave the target price to 21.3, respectively 10.8/9.2x P/E for 2015/2016. 'Buy' rating.

(Financial figures as at 7 August 2015)

Buy (Initiation)

CMP CNY 17.14

(Closing price as at 7 August 2015)

TARGET CNY21.3 (+24%)

COMPANY DATA

O/S SHARES (MN) :	2583
MARKET CAP (CNY MN) :	44689
52 - WK HI/LO (CNY):	25.67/ 11.24

SHARE HOLDING PATTERN, %

SAIC	60.1
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PRICE PERFORMANCE, %

	1month	3month	1year
HASCO	-4.41	-15.5	40.2
SHCOMP index	-1.38	-2.08	-25.11

PRICE VS. SHCOMP



Source: Phillip Securities (HK) Research

KEY FINANCIALS

CNY mn	FY13	FY14	FY15E	FY16E
Net Sales	69558	73756	90856	108057
Net Profit	3448	4456	5099	5992
EPS, CNY	1.33	1.72	1.97	2.32
P/E, x	12.8	9.9	8.7	7.4
BVPS, CNY	7.21	9.14	10.38	11.99
P/BV, x	2.4	1.9	1.7	1.4
DPS (CNY)	0.47	0.52	0.60	0.70
Div. Yield (%)	2.7%	3.0%	3.5%	4.1%

Source: Company reports, Phillip Securities Est.

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Company Profile

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Hasco's Business Segment



Source: Company, Phillip Securities Hong Kong Research

The Company was previously under the auto components business of SAIC. In order to develop a more competitive and independent value chain of auto components, SAIC injected the auto component business from Shanghai Bashi Industrial Group (SBIG) during its restructuring in May 2009. SBIG was subsequently renamed HASCO and is 60.1% owned by SAIC. It becomes the key auto components platform of SAIC.

HASCO has 31 directly invested companies in total, including world renowned enterprises such as Yanfeng Visteon Automotive Trim Systems Co., Ltd., Shanghai Koito Automotive Lamp Co., Ltd., Shanghai Valeo Automotive Electrical Systems Co., Ltd., Shanghai Sanden Behr Automotive Air Condition Co., Ltd., Shanghai GKN Drive Shaft Co., Ltd., ZF Shanghai Steering Systems Co., Ltd. As its customers are more concentrated, its top 5 customers contributed to 62.5% of total sales in 2014. HASCO has 62 related companies which are awarded the status of 'high-tech enterprises'.

Three Core Competitive Advantages to Secure its Leading Position

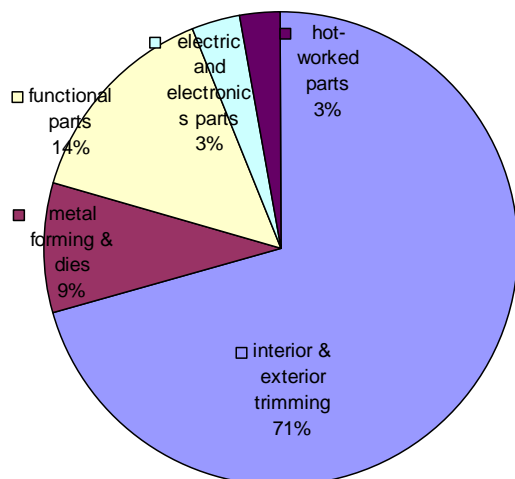
HASCO is the pioneer of China's auto component industry. It is a listed integrated auto parts and components supplier, with the largest production capacity, the most comprehensive product offering, the broadest customer coverage and the strongest R&D capability in China. Many of its joint ventures companies, which are set up by SAIC with the world's leading auto parts and components players, are the leaders in their respective sub-segments.

The major customers of the company are top auto manufacturers in China. It has established stable and long-term strategic relationships with SAIC, FAW Group, DFPSA, Chang'an Automobile, GAC, BAIC Group, BMW Brilliance, Great Wall Motor, JAC Motors, etc. The company possesses an integrative competitiveness in quality, service, technology and price (QSTP) and hence attaining a higher profitability than the industry average.

HASCO has built up a rather comprehensive supply chain of auto parts and components. As of the end of 2014, the subsidiaries and related companies of HASCO have established 261 R&D, manufacturing and service bases in China. 14 manufacturing bases have also been set up in various overseas countries, such as USA, Germany, Thailand, Russia, Australia, Czech and India. As its businesses sprawl across broad segments that cover both the Chinese and overseas market, it starts to enjoy the benefits of clustering effects.

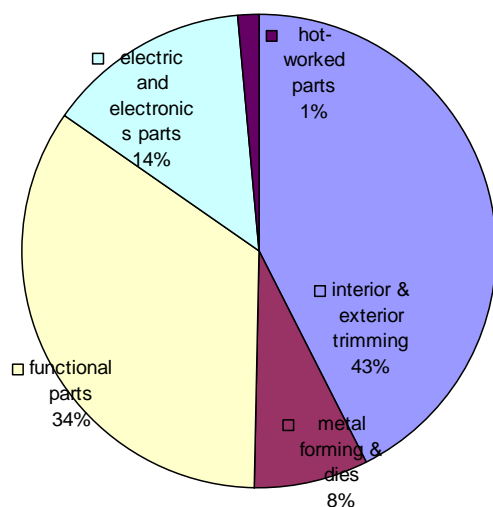
As for breakdown of profit by business lines, functional parts and interior & exterior trimming parts are the two largest profit contributors, accounting for 43% and 36% of total profits. Electronic and electric parts rank the third with 10% of profit contribution. Metal forming and dies / molds and hot working parts account for a total of 10% profit. As for the breakdown of profit contribution by invested companies, Yanfeng Visteon Automotive Trim Systems is the major profit centre, contributing to over 70% of HASCO's sales revenue and 47% of net profit.

Revenue breakdown by Segments



Source: Company, Phillip Securities Hong Kong Research
(Financial figures as at 7 August 2015)

Profit breakdown by Segments



Source: Company, Phillip Securities Hong Kong Research

(Financial figures as at 7 August 2015)

Steady Progress of `Post-JV era` Strategic Transformation

Through the competitive advantage of forming long-term partnership with global auto parts leaders, HASCO has set up a clear strategy of `Zero level, neutral, Global`. It has gradually identified and prioritized foci of its future development, namely: the company will continue grow its core businesses through a combination of outward expansion and organic growth, so that it can foster transformation and upgrade of these business lines to support sustainable growth. The completion of acquiring 50% stake in Yanfeng Visteon Automotive Trim Systems in 2013 signaled that the company has entered into a `Post-JV` strategic transformation.

As China's overall auto sales growth steadily slows down, demand for quality auto products will gradually increase. Competition among auto manufacturers will become fiercer. To attract customers, auto manufacturers will tend to apply more high-end and high-technology auto parts and components in their automobiles. This trend will certainly benefit top-tier auto parts manufacturers such as HASCO. In an industry where impact of the economies of scale is significant, companies' profit can be improved through the increase in market share.

Besides, HASCO plans to strengthen the partnership and restructuring of the global interior trimming parts business of Johnson Controls. The ultimate plan is to set up the world's largest interior trimming parts company, with HASCO holding a 70% stake to secure its leading global position in the business. While its overseas business just accounts for a small portion of the total business with 1.6% revenue contribution, we look forward to its future growth potential.

Valuation

As analyzed above, we revised EPS expectation of the Company to RMB 1.97 and 2.32 of 2015/2016. And we accordingly gave the target price to 21.3, respectively 10.8/9.2x P/E for 2015/2016. `Buy` rating.

Peer Comparison

Ticker	Name	Market Cap (HKD)	BEST P/B	BEST P/B:2F Y	BEST P/E:1F Y	BEST P/E:2FY	BEST EV/BEst EBITDA	P/B	ROA	LF	ROE
CNY											
600741 CH Equity	HUAYU AUTOMOTIVE	55012	1.7	1.4	9.0	7.9	7.4	1.8	7.5	20.8	
000559 CH Equity	WANXIANG QIANCH	58798	N/A	N/A	57.0	52.6	N/A	11.3	6.6	18.7	
600660 CH Equity	FUYAO GROUP GLAS	41316	2.1	1.9	12.3	10.6	7.6	2.4	14.1	22.3	
000581 CH Equity	WEIFU HIGH-TECHN	33818	2.3	2.0	14.1	11.5	18.4	2.5	10.6	14.4	
601311 CH Equity	CAMEL GROUP CO LT	22995	3.5	3.2	22.1	16.8	16.6	4.6	12.0	17.9	
600742 CH Equity	CHANGCHUN FAWAY	6786	N/A	N/A	8.3	7.3	N/A	1.5	8.7	15.6	
EUR (2 securities)											
CON GR Equity	CONTINENTAL AG	374199	3.5	2.9	15.5	14.1	8.2	3.7	8.1	23.2	
EO FP Equity	FAURECIA	38951	2.2	1.9	12.7	10.3	4.0	2.3	2.5	13.3	
GBp (1 security)											
GKN LN Equity	GKN PLC	66393	3.9	3.4	12.0	10.9	7.0	3.4	2.3	9.2	
JPY (3 securities)											
6902 JP Equity	DENSO CORP	338884	1.5	1.4	16.4	14.9	7.7	1.5	6.2	9.9	
7259 JP Equity	AISIN SEIKI CO LTD	93931	1.1	1.1	14.4	12.7	4.9	1.2	2.7	6.9	
3116 JP Equity	TOYOTA BOSHOKU C	27602	1.9	1.8	22.0	19.1	6.1	2.0	1.6	5.0	
KRW (1 security)											
012330 KS Equity	HYUNDAI MOBIS CO	133086	0.8	0.7	6.2	5.8	4.4	0.8	8.8	15.0	
USD (6 securities)											
JCI US Equity	JOHNSON CONTROLS	235252	2.6	2.4	13.6	11.8	9.8	2.9	4.7	13.6	
MGA US Equity	MAGNA INTERNATIONAL	177890	2.0	2.0	12.0	9.9	7.1	2.7	10.7	21.5	
DLPH US Equity	DELPHI AUTOMOTIVE	170800	8.6	6.0	14.5	12.2	9.4	8.9	13.5	53.5	
BWA US Equity	BORGWARNER INC	83785	3.0	2.7	15.6	13.1	8.4	2.9	8.3	16.9	
LEA US Equity	LEAR CORP	61601	2.6	2.2	10.4	9.2	5.7	2.7	7.8	24.2	
VC US Equity	VISTEON CORP	31656	1.3	1.6	50.8	32.7	6.9	1.5	39.7	105.0	

Source: Company, Phillip Securities Hong Kong Research

(Financial figures as at 7 August 2015)

Financials

FYE DEC	FY11	FY12	FY13	FY14	FY15F	FY16F
Valuation Ratios						
P/E (X), adj.	14.8	14.3	12.8	9.9	8.7	7.4
P/B (X)	2.7	2.3	2.4	1.9	1.7	1.4
Dividend payout ratio(%)	25.9%	30.8%	35.2%	30.1%	30.4%	30.2%
Dividend Yield (%)	1.8%	2.2%	2.7%	3.0%	3.5%	4.1%
Per share data (RMB)						
EPS, (Basic)	1.16	1.20	1.33	1.72	1.97	2.32
EPS, (Diluted)	1.16	1.20	1.33	1.72	1.97	2.32
DPS	0.30	0.37	0.47	0.52	0.60	0.70
BV/PS	6.41	7.46	7.21	9.14	10.38	11.99
Growth & Margins (%)						
Growth						
Revenue	16.5%	10.6%	20.5%	6.0%	23.2%	18.9%
EBIT	18.1%	6.2%	4.2%	-8.3%	28.1%	19.2%
Net Income, adj.	17.1%	3.8%	11.1%	29.2%	14.4%	17.5%
Margins						
Gross margin	16.0%	16.1%	15.4%	15.2%	15.4%	15.4%
EBIT margin	7.8%	7.5%	6.5%	5.6%	5.8%	5.9%
Net Profit Margin	5.7%	5.4%	5.0%	6.0%	5.6%	5.5%
Key Ratios						
ROE	19.2%	17.3%	18.2%	21.1%	20.2%	20.7%
Income Statement (RMB mn)						
Revenue	52177	57733	69558	73756	90856	108057
Gross profit	8327	9277	10698	11199	13983	16641
EBIT	4086	4338	4519	4142	5306	6327
Profit before tax	5943	6222	7170	6982	8218	9523
Tax	597	676	842	786	929	1095
Profit for the period	5345	5546	6328	6196	7289	8428
Minority interests	2355	2442	2880	1740	2190	2436
Total capital share	2583	2583	2583	2583	2583	2583
Net profit	2990	3103	3448	4456	5099	5992

Source: PSR

(Financial figures as at 7 August 2015)

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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