EQUITY RESEARCH

FDG (729.HK)

Teleconference Takeaways

China | Automobile | Company Updates

Company Profile

FDG Electric Vehicles Limited is an integrated electric vehicle manufacturer and is mainly engaged in (i) independent R&D, design and production of electric vehicles; (ii) R&D, production and sales of lithium-ion batteries and related products; (iii) R&D, manufacturing and sales of cathode materials for the production of lithium-ion batteries; and (iv) electric vehicle rental and direct investment.

What`s New

We participated in the reverse roadshow organized by the company, visited and researched the company`s Changjiang Auto Engine Factory located in Hangzhou, Zhejiang Province, and published a research summary in mid-April. For details, please see our research report published on May 29. The company recently announced its result report of the fiscal year 2017 and 2018, with a loss of 2.23 billion in the attributable net income.

Takeaways from the teleconference

In order to understand the company`s latest progress, we had a conference call with the company`s management. The minutes are as follows:.

Q1, The share price of CAR Inc. is only about 46.5% of it before the suspension announcement. How does the management consider the reason why the cut-rate price is so high?

A: As the founder and manager, the management of the company was not willing to make too much dilution on the share capital. The past year was full of challenge for the company due to the influence of the macropolicy and other factors. The interruption of the subsidy policy almost stopped the company`s sales in the first half of 2017. The new subsidy policy requires the company to meet the threshold of 20,000 kilometres, and the time of receiving the subsidy is still too long. However, since the company`s products were only sold to the domestic market in 2017, and the first batch of products were not sold to the United States until the second half of 2017. The domestic products are mostly premium, and they are generally used for corporate reception and other purposes after purchased by the domestic customers, which makes the time of receiving subsidy longer. All these reasons are putting a lot of pressure on the company`s payment collection. CAR Inc. is China`s largest and most recognized car rental service provider, and it is in an absolute leading position in the Chinese car rental industry in terms of fleet size, outlet coverage, market share and business income and other operation and financial indicators. Under the consensus of the irreversible electrification trend in the auto industry, the synergistic effect would be released and created for both parties in the future with the use of the knowledge, networks and assets of the two companies; in the short term, it will also provide valuable and timely help for the company to repay debts and supplement operating capital.

3 August 2018

No Rating

CMP HKD 0.099

Target price: N/A

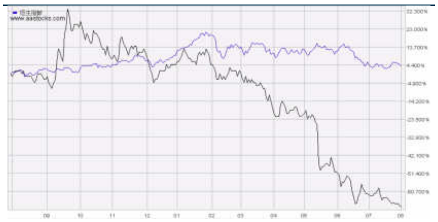
COMPANY DATA

O/S SHARES (MN) :	23413
MARKET CAP (HKD MN) :	2318
52 - WK HI/LO (HKD):	0.435/0.098

SHARE HOLDING PATTERN, %

Mr Cao Zhong	5.8
CITIC International Assets Management Ltd	10.6
Mr Miao Zhenguo	4.3

PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

HKD mn	FY15	FY16	FY17	FY18
Net Sales	304	363	1513	1058
Net Profit	(410)	(228)	(555)	(2230)
EPS	(0.02)	(0.01)	(0.03)	(0.10)
P/E, x	(5.0)	(9.9)	(3.3)	(1.0)
BVPS,	0.12	0.15	0.13	0.05
P/BV, x	0.9	0.6	0.8	2.0
DPS	0.00	0.00	0.00	0.00
Div. Yield (%)	0.0%	0.0%	0.0%	0.0%

Source: Company reports, Phillip Securities Est.

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Q2, CAR Inc. mainly rents and operates passenger cars. Will it be different from the company`s main orientation of producing electric commercial vehicles?

A: FDG is focusing on the B2B commercial vehicle market. Hangzhou Changjiang, a subsidiary of FDG, has been a dual-qualified company granted by the Ministry of Industry and Information Technology and the National Development and Reform Commission for the qualification of new energy passenger vehicles. CAR Inc. is Asia`s largest fleet rental service provider. The company can manufacture electric passenger cars for CAR Inc., which belong to the B2B electric car market and they are also the electric passenger cars. Hangzhou main engine factory of FDG is currently only built in one phase, covering an area of 700 mu and investing 2.5 billion yuan. It is equipped with the entire industrial chain of electric vehicles such as stamping, welding, painting, final assembly and electronic control. The designed production capacity is 100,000 units, of which 20 thousand vehicles are commercial vehicles, including medium/large electric buses/logistics vehicles, and 80,000 units are reserved for electric passenger vehicles. The company also produced small SUV passenger cars. At the Beijing Auto Show in April this year, there were three pure electric passenger cars in the FDG exhibits, including one mid-size sedan, one mid-size SUV and one concept car.

Q3, If the issuance of additional shares is successful, will the corporate management style be different? What kind of changes will it bring to the company?

If the additional issuance is successful, the Board of Directors may be restructured, but we believe that the company`s operation and management will remain unchanged. General Manager Cao is still the main controller of Hangzhou Changjiang Auto Co., Ltd., a subsidiary and core asset of FDG. The management will not change too much. CITIC was also one of the major shareholders, but it did not interfere with the company`s operations.

Q4, Could you please collate the previous and recent production and overseas orders?

A: In the 2017 and 2018 fiscal year, the company sold about 800 electric vehicles, mainly sold in the second half of the year, because the entire industry was affected by the subsidy decline and not so much cars were sold out in the first half of the year. Among them, the cars were mainly sold to the domestic customers in the 2017 and 2018 fiscal year, and about 1,200 units were sold in the previous fiscal year of 2016/17. In the second half of 2017/18, the company`s products finally obtained the U.S. certification. And 125 units were exported to the renowned American logistics vehicle operator Ryder (NYSE: R) by the company for the first time. Recently, Ryder has added an order of 500 units, fully illustrating the product competitiveness of the company and customer recognition of the company`s products.

Q5, In the 17/18 fiscal year, there was a huge loss of 2.23 billion, which was much higher than the profit warning in May. We saw a significant increase in the value of the impairment. Is it possible to rush back in the future with government subsidies in place?

A: Among the 1.4 billion trade and bill receivables of the company, up to 680 million are unfunded government subsidies. Based on the conservative principle, the auditors also made impairment losses for some government subsidies receivables, which is included in the 2.7 billion trade receivables impairment. The company believes that some of the accounts receivables of the company are possible to retrieve in the future.

Q6, Why is there a decline in the cathode material business in the second half of the fiscal year?

A: The company`s cathode materials are mainly produced and sold by its subsidiary FDG Power (378.HK). Our sales are limited mainly by the high price fluctuation of raw materials and tightened credit control for existing customers. In addition, changes in the subsidy policy for new energy buses have led to changes in demand for lithium iron phosphate battery products, thus resulting in the changes in the demand for cathode materials. The company totally holds approximately 75% of the equity of FDG Power. FDG Power has signed an agreement with customers on March 26, 2018 to transfer the production capacity of the Chongqing base (the main cathode material production base) to a third party. The production capacity in 2018 has been fully implemented and a stable income stream will be obtained. Its production capacity is nearing full, contributing a stable gross profit margin to the Group.

Q7, It is announced in the company report that the company would change the previous vertical longitudinal integration business model and shift its focus to the hard-core and high-margin electric commercial vehicle manufacturing. What arrangements will be made for other non-core businesses (batteries and cathode materials)?

A: In view of the rapid development of the new energy vehicle industry market today, the longitudinal vertical integration business model is not optimal. Outsourcing the supply chain can fully share the advantages of specialized production. The company`s previous sale of the poorly profitable Yunnan business was the beginning of focusing on the core business. After years of investment and cultivation, the company`s core business in electric commercial vehicle has been ready. As for some non-core businesses, the company will consider and not limited to the introduction of strategic investors, divestiture and other methods to integrate, in order to concentrate resources to develop core business.

Q8, Do you have any latest developments and plans for overseas markets?

A: In 2015, the company established the jointly owned company Chanje in the United States, and the electric commercial vehicle obtained the U.S.-certified sales qualification in 2017. Since the delivery of 125 probationary units to Ryder in the last fiscal year, 500 additional orders are obtained this year, which are delivered to a large U.S. blue-chip company serviced by Ryder to further confirm the durability of the products. If it goes well, it is expected to obtain a larger batch of orders, and a brand demonstration effect can be formed to attract a larger customer base. The company is now promoting the plan of the SKD plant in the United States and it will also accelerate its progress in response to the possible Sino-U.S. trade war. After entering the U.S. market through the blue-chip logistics company, the group will enter Europe with the help of the global layout of these companies. Because the European market is the next market that may achieve rapid electrification, and the company`s development can also enter a virtuous cycle.

Financials

FYE DEC	FY03/12	FY03/13	FY03/14	FY03/15	FY03/16	FY03/17	FY03/18
Valuation Ratios							
P/E (X), adj.	(2.5)	(3.3)	(1.4)	(5.0)	(9.9)	(3.3)	(1.0)
P/B (X)	2.1	3.6	1.0	0.9	0.6	0.8	2.0
Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Dividend payout ratio (%)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Per share data (HKD)							
EPS, reported	(0.04)	(0.03)	(0.07)	(0.02)	(0.01)	(0.03)	(0.10)
EPS, adj.	(0.04)	(0.03)	(0.07)	(0.02)	(0.01)	(0.03)	(0.10)
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00
BVPS	0.05	0.03	0.10	0.12	0.15	0.13	0.05
Growth & Margins (%)							
Growth							
Revenue	-23.1%	-7.0%	54.0%	270.8%	19.7%	316.4%	-30.0%
EBIT	NA	-32.5%	157.4%	-51.1%	28.1%	-26.9%	73.1%
Net Income, adj.	NA	-26.7%	179.4%	-54.8%	-44.3%	143.2%	302.0%
Margins							
Gross margin	4.4%	12.3%	5.9%	23.2%	39.7%	32.5%	32.5%
EBIT margin	NA	-674.1%	-1127.0%	-148.6%	-159.0%	-27.9%	-27.9%
Net Profit Margin	NA	-610.1%	-1107.1%	-135.0%	-62.8%	-36.7%	-36.7%
Key Ratios							
ROE (%)	-86.2%	-74.6%	-87.41%	-21.54%	-8.40%	-17.58%	-108.34%
ROA (%)	-24.3%	-19.1%	-32.93%	-8.28%	-3.10%	-5.68%	-20.76%
Income Statement (HKD mn)							
Revenue	**57**	**53**	**82**	**304**	**363**	**1,513**	**1,058**
Gross profit	55	47	77	233	219	1,021	917
Operating expense	(119)	(137)	(127)	(448)	(588)	(384)	(1,753)
EBIT	(123)	(145)	(140)	(527)	(755)	(1,066)	(1,933)
Profit before tax	(546)	(376)	(937)	(567)	(889)	(742)	(3,163)
Tax	(103)	(52)	(25)	(58)	(1)	(17)	(96)
Profit for the period	(442)	(324)	(912)	(509)	(888)	(725)	(3,067)
Minority interests	0	0	(5)	(99)	(660)	(170)	(837)
Total capital share	10,992	12,255	16,977	17,866	21,964	22,398	22,413
Net profit	**(442)**	**(324)**	**(906)**	**(410)**	**(228)**	**(555)**	**(2,230)**

Source: PSR

(**Financial figures as at 1 August 2018**)

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 ± 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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