

# GAC (2238 HK)

## The Upgrade of Self-owned Brands start again

Hong Kong | Automobile | Update Report

### 50% Decrease in Result in the Third Quarter

In Q3 2019, GAC recorded operating revenue of RMB14,561 million, down by 9.65% yoy; the net profit attributable to the parent company was RMB1,416 million, down by 52% yoy, and down by 34% qoq. During the first three quarters, GAC recorded operating revenue of RMB42,684 million, down by 19.2% yoy; the net profit attributable to the parent company was RMB6,335 million, down by 35.75% yoy. The decrease in result in Q3 was higher than that of Q1 and Q2 by 29% and 30%, respectively.

### Profitability Affected by De-inventory under Transformation of Emission Standards

The gross margin in Q3 was 6.1%, down by 12.5 ppts yoy, mainly due to the bigger promotion to clear the inventory of China V vehicles, the sharp decline of Trumpchi SUV affected by depression of domestic SUV market, as well as the loss of new energy vehicles business at the picking-up period. In Q3, the sales of Trumpchi was 90,000 units, down by 28.6% yoy, and worse than the average level of the industry. The Company strictly controlled the expenses. The sales/administration/financial expenses ratio decreased by 0.4 ppts to 11.43%, totalling RMB1.68 billion. Due to the large investment into new vehicles and new platforms, the R&D expenses increased by 100% to RMB0.38 billion.

### Japanese Brands Exceed Expectation and American Brands are Weak, with the Same Return on Investment

The sales volume of GAC Toyota in Q3 was 185,000 units, up by 11.1% yoy; the sales volume of GAC Hongda was 179,000 units, down by 1.6% yoy; the sales momentum of hot models like Camry/Highlander/Accord was well. The sales volume of GAC Mitsubishi Motors increased by 3% yoy, and the sales volume of GAC FCA decreased by 39% yoy, but rebounded by 7% and 17% compared with Q2, respectively. The investment gain was RMB2.55 billion, down by 0.4% yoy, and up by 6.6% qoq.

### The Upgrade of Self-owned Brands start again

The brand image and product reputation of Trumpchi of GAC have been established during ten years of development. Under the decline pressure of the economy, the domestic passenger vehicle market, especially the self-owned brands, will be increasingly difficult to continue the previous high growth. In order to adapt the competition of the vehicle market in the adjustment period in the next two or three years, the Management of the Company will make preparations and integrate resources to improve the competitiveness of Trumpchi from the following aspects: 1) focusing on the reliable quality and design of products, 2) strengthening the integration and linkage of R&D and production, 3) speeding up the construction of intelligent internet connection and new energy technology system, 4) improving the sales system comprehensively, 5) promoting the reform of professional manager and mixed ownership. The sales volume of new energy strategic model AionS was 14,000 units as of the end of September, with orders for 50,000 units in hand; in October, new vehicle AionLX will be launched with superiorities, such as position as a supercar SUV, installation with ADiGO (smart driving internet) ecosystem and L3 automatic assistance driving system, as well as comprehensive endurance exceeding 600 km, which is expected to promote GAC to win reputation and to improve product mix.

18 November 2019

### Accumulate (Downgrade)

CMP HKD 8.17

(Closing price as at 14 November)

TARGET HKD 8.9 (+9%)

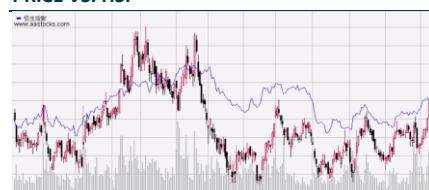
#### COMPANY DATA

O/S SHARES (MN):	10231
MARKET CAP (HKD MN):	25316
52 - WK HI/LO (HKD):	10.6 / 6.95

#### SHARE HOLDING PATTERN, %

Guangzhou Automobile Industry Group Co., Ltd	60.63
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#### PRICE VS. HSI



Source: Phillip Securities (HK) Research

#### KEY FINANCIALS

CNY mn	FY17	FY18	FY19E	FY20E
Net Sales	71,575	72,380	60,979	65,723
Net Profit	11,005	10,900	7,824	9,103
EPS, CNY	1.68	1.07	0.76	0.89
P/E, x	4.1	6.7	9.5	8.2
BVPS, CNY	10.60	7.49	7.88	8.37
P/BV, x	0.7	1.0	0.9	0.9
DPS (CNY)	0.53	0.38	0.30	0.35
Div. Yield (%)	7.7%	5.3%	4.1%	4.8%

Source: Company reports, Phillip Securities Est.

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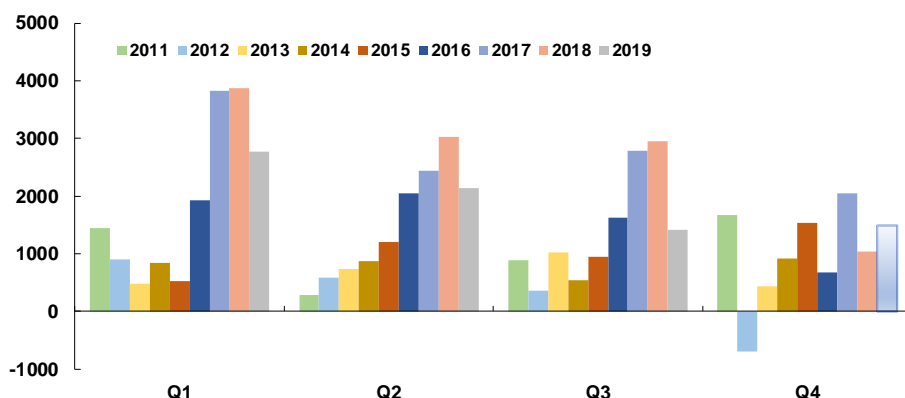
### Production Expansion of Japanese Brands Imminently

We expect that the strong momentum of Japanese brands will continue, and the blockbuster models Haoying of GAC Hongda and Willanda of GAC Toyota to be launched at the end of the year will continue to enhance the product matrix of joint ventures. The production expansion project of GAC Toyota and GAC Hongda is expected to be put into production at the end of the year. Each of the production capacity will increase by 120,000 to 240,000 units, which will accumulate strength for the development in the next stage.

### Investment Thesis

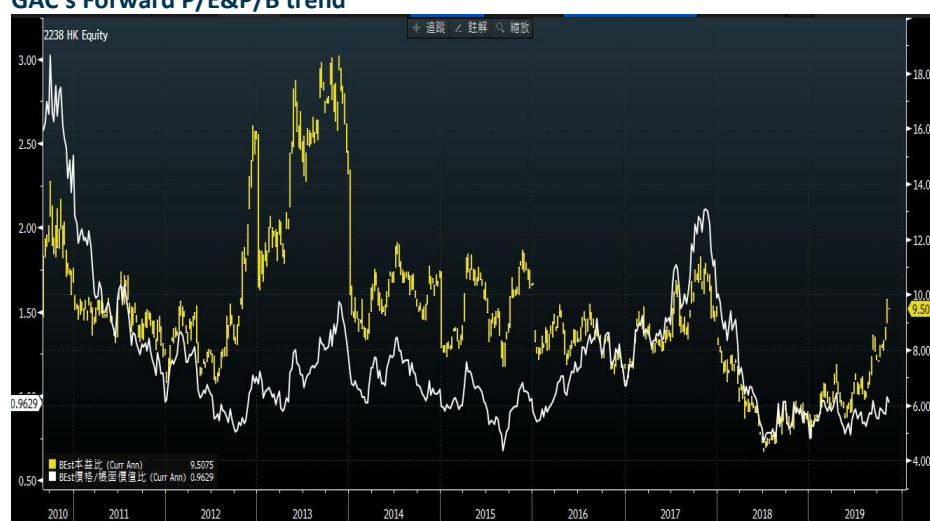
Thanks to the strong momentum of GAC Toyota/GAC Honda, the Company's result safety mat is thicker; the self-owned brands are expected to gradually stabilize and rebound under the help of the new generation models and new energy models. We revised the Company's 2019/2020 earnings forecast. We give the "Accumulate" rating with the target price to HKD 8.9, equivalent to 10.4/8.9x P/E and 1.0/0.9x P/B ratio in 2019/2020. (Closing price as at 14 November)

### GAC's quarterly net profit



Source: Wind, Phillip Securities Hong Kong Research

### GAC's Forward P/E&P/B trend



Source: Bloomberg, Phillip Securities Hong Kong Research

## Financials

FYE DEC	FY15	FY16	FY17	FY18	FY19F	FY20F
<b>Valuation Ratios</b>						
P/E (X), adj.	10.5	7.5	4.1	6.7	9.5	8.2
P/B (X)	1.1	1.1	0.7	1.0	0.9	0.9
Dividend payout Yield (%)	30.6%	32.1%	32.2%	35.9%	39.3%	39.5%
Dividend Yield (%)	2.9%	4.2%	7.7%	5.3%	4.1%	4.8%
<b>Per share data (RMB)</b>						
EPS, reported	0.65	0.98	1.68	1.07	0.76	0.89
EPS, adj.	0.65	0.97	1.65	1.06	0.76	0.89
DPS	0.20	0.31	0.53	0.38	0.30	0.35
BVPS	6.01	6.81	10.60	7.49	7.88	8.37
<b>Growth &amp; Margins (%)</b>						
<b>Growth</b>						
Revenue	31.5%	68.0%	44.8%	1.1%	-15.8%	7.8%
EBIT	39.8%	58.2%	67.6%	-5.4%	-34.3%	18.4%
Net Income, adj.	32.2%	49.3%	75.0%	-1.0%	-28.2%	16.3%
<b>Margins</b>						
Gross margin	11.7%	15.1%	18.0%	15.9%	9.1%	11.4%
EBIT margin	16.0%	15.0%	17.4%	16.3%	12.7%	13.9%
Net Profit Margin	14.3%	12.7%	15.4%	15.1%	12.8%	13.9%
<b>Key Ratios</b>						
ROE (%)	11.4%	15.2%	19.4%	14.9%	10.0%	10.9%
ROA (%)	6.5%	8.4%	10.9%	8.7%	5.9%	6.7%
<b>Income Statement (RMB mn)</b>						
Revenue	29418	49418	71575	72379.8	60979	65723
Gross profit	3444	7456	12858	11544	5561	7486
EBIT	4696	7427	12445	11773	7734	9161
Profit before tax	4386	7050	12194	11863	7875	9320
Tax	-400	-754	-1154	-921	66	-73
Profit for the period	3986	6295	11040	10942	7941	9247
Minority interests	-226	8	35	43	117	144
Total capital share	6435	6439	6551	10231	10231	10231
Net profit	4212	6288	11005	10900	7824	9103

Source: PSR

(Closing price as at 14 November)

### 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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