

Brilliance China Automotive

Read-through from BMW's FY14 results

BMW released its FY14 annual report today. Brilliance BMW's solid net profit of €1,339mn (up 61% YoY) implies Brilliance-BMW JV's 2H14 profit could top Rmb1.8-1.9bn, bringing Brilliance China's FY14 earnings to Rmb5.3-5.4bn, 4-6% above JPM/consensus estimates of Rmb5.1-5.2bn. Brilliance remains one of our four top picks in China along with Geely Auto. (Please note BMW, OW rating, is covered by our European Auto Head, Jose Asumendi. Click [here](#) for Jose's latest views).

- Read-through of BMW's FY14 results:** BMW reported €655mn equity income consisting of two JVs: 1) Brilliance China which contributed to €670mn equity income and 2) DriveNow, a car-sharing provider which recorded a minor loss in FY14. Further taking into account of Brilliance's contained loss in its own brand mini-bus business, we believe Brilliance China's bottom line in 2H14 could reach ~Rmb1.6bn, bringing full-year profit to ~Rmb5.3-5.4bn and beating our estimate by 4-6%. We have been bullish on Brilliance and our Rmb5.1bn forecast has been above the Street since Aug-14 (see [here](#)) while the consensus estimate has been catching up from Rmb4.5bn since then.
- Our bullish view on Brilliance:** We remain optimistic on Brilliance and expect ~20% sales volume growth in FY15 despite the next new model will only be launched in 4Q15. X1 compact SUV and 3-series sedan (including its likely facelift in 2H15) should lead the momentum this year. On the bottom line, we believe 11% net margin assumption is conservative and achievable. We are looking for 19% earnings growth next year vs. consensus of 14%.
- Earnings estimate revisions:** We tweak Brilliance China's FY14/15 estimates slightly to reflect the solid result from Brilliance BMW. Our FY15 estimate is now 8% above consensus.
- Rating, risks:** We retain our OW on Brilliance and our Dec-15 PT of HK\$19. Key risks to our call include worse-than-expected sales/profit and a sharper-than-expected price cut in China's auto market, including luxury segment where Brilliance focuses.

Brilliance China Automotive (Reuters: 1114.HK, Bloomberg: 1114 HK)

Rmb in mn, year-end Dec	FY12A	FY13A	FY14E	FY15E	FY16E
Revenue (Rmb mn)	5,916	6,103	6,033	6,102	6,099
Net Profit (Rmb mn)	2,301	3,374	5,298	6,312	7,219
EPS (Rmb)	0.46	0.67	1.05	1.26	1.44
DPS (Rmb)	0.00	0.00	0.08	0.08	0.10
Revenue growth (%)	(8.2%)	3.2%	(1.2%)	1.1%	(0.0%)
EPS growth (%)	26.3%	46.6%	57.0%	19.1%	14.4%
ROE	27.1%	29.3%	37.9%	35.4%	29.9%
P/E (x)	26.8	18.3	11.7	9.8	8.6
P/BV (x)	6.2	4.7	4.2	3.0	2.2
Dividend Yield	0.0%	0.0%	0.7%	0.7%	0.8%

Source: Company data, Bloomberg, J.P. Morgan estimates.

Overweight

1114.HK, 1114 HK

Price: HK\$15.26

Price Target: HK\$19.00

China

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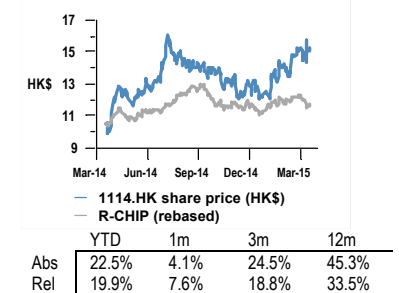
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Price Performance



Company Data

Shares O/S (mn)	5,026
Market Cap (Rmb mn)	61,746
Market Cap (\$ mn)	9,880
Price (HK\$)	15.26
Date Of Price	18 Mar 15
Free Float(%)	57.4%
3M - Avg daily vol (mn)	10.34
3M - Avg daily val (HK\$ mn)	144.95
3M - Avg daily val (\$ mn)	18.7
R-CHIP	4463.24
Exchange Rate	7.76
Price Target End Date	30-Dec-15

See page 7 for analyst certification and important disclosures, including non-US analyst disclosures.

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<p>Key catalysts for the stock price: Strong sequential volume growth from 3-series and X1 following completion of Teixi plant expansion in Oct-13.</p>	<p>Upside risks to our view: On BMW JV: better-than-expected sales and higher-than-expected margins of BMW cars; stronger-than-expected sales momentum in luxury segment resulting from solid growth in China's household income. On minivan: smaller-than-expected loss from higher sales and lower expenses.</p>	<p>Downside risks to our view: Key risks include weaker-than-expected sales volume of BMW's cars in China, and a sharper-than-expected price cut in China's auto market, including luxury segment where Brilliance focuses. We are also cautious on any higher-than-anticipated loss from mini bus and future new energy car business.</p>
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Key financial metrics	FY13	FY14E	FY15E	FY16E
Revenues (LC)	6,103	6,033	6,102	6,099
Revenue growth (%)	3%	-1%	1%	0%
EBITDA (LC)	(39)	68	68	81
EBITDA margin (%)	-1%	1%	1%	1%
Tax rate (%)	0%	0%	2%	6%
Net profit (LC)	3,374	5,298	6,312	7,219
EPS (LC)	0.67	1.05	1.26	1.44
EPS growth (%)	47%	57%	19%	14%
DPS (LC)	-	0.08	0.08	0.10
BVPS (LC)	2.59	2.95	4.14	5.47
Operating cash flow (LC mn)	(154)	(323)	(52)	(670)
Free cash flow (LC mn)	(602)	(773)	(500)	(1,118)
Interest cover (X)	26	37	44	51
Net margin (%)	55%	88%	103%	118%
Sales/assets (X)	0.35	0.30	0.26	0.20
Debt/equity (%)	13%	12%	9%	7%
Net debt/equity (%)	-5%	-3%	-5%	-1%
ROE (%)	29%	38%	35%	30%

Key model assumptions	FY13	FY14E	FY15E	FY16E
BMW sales volume growth	29%	35%	21%	21%
BMW gross margin	24%	26%	26%	26%
BMW net margin	9%	11%	11%	11%

Source: Bloomberg, Company data and J.P. Morgan estimates.

Sensitivity analysis	Impact on EBIT (%)		Impact on EPS (%)	
Sensitivity to	FY14E	FY15E	FY14E	FY15E
1% decrease in BMW sales volume growth	-1.1%	-0.9%	-1.2%	-0.9%
1% decrease in BMW gross margin assumption	-1.0%	-1.0%	-1.0%	-1.0%

Source: J.P. Morgan estimates.

China auto valuation summary

Company	Code	Rec	Price (LC)		Mkt cap (US\$ M)	P/E (x)		P/B (x)		ROE		Div. yield	
			18-Mar			14E	15E	14E	15E	14E	15E	14E	15E
Brilliance	1114 HK	OW	15.26		9,885	11.6	9.7	4.1	2.9	38%	35%	0.7%	0.7%
ZhengTong Auto	1728 HK	OW	3.82		1,088	6.5	5.3	0.8	0.7	13%	14%	2.6%	3.1%
DongFeng Motor	489 HK	OW	12.08		13,415	6.4	5.5	1.1	1.1	19%	19%	1.9%	2.7%
Great Wall Motor	2333 HK	OW	48.65		22,593	15.7	11.0	3.5	2.8	24%	29%	2.1%	1.9%
Geely	175 HK	OW	3.60		4,084	17.7	9.6	1.4	1.3	8%	14%	1.3%	0.5%
GAC	2238 HK	UW	7.17		8,687	11.8	9.8	1.0	1.0	9%	10%	2.8%	3.4%
MintH Group	425 HK	N	13.90		1,970	10.7	9.6	1.4	1.3	14%	14%	3.2%	3.3%
Baoxin Auto	1293 HK	N	4.42		1,457	8.4	7.3	1.6	1.3	21%	19%	3.4%	3.6%
Zhongsheng	881 HK	UW	5.52		1,527	8.4	7.0	1.0	0.9	13%	13%	2.2%	2.2%
Sinotruk	3808 HK	UW	4.41		1,569	20.3	14.9	0.5	0.5	3%	3%	0.9%	1.5%
Nexteer	1316 HK	OW	8.03		2,585	16.0	12.6	3.8	3.0	26%	27%	0.0%	0.8%
Sunfonda	1771 HK	UW	3.18		246	6.0	5.9	0.8	0.8	17%	14%	0.0%	0.0%
SAIC Motor	600104 CH	OW	25.16		44,531	9.9	8.8	1.8	1.6	19%	20%	4.8%	5.4%
Weichai Power (1)	2338 HK	OW	28.60		8,778	10.5	9.0	1.5	1.3	15%	15%	1.3%	1.6%
BYD (2)	1211 HK	OW	37.65		17,809	146.3	28.8	2.6	2.3	2%	10%	0.0%	0.0%
Average (3)						12.5	10.2	1.7	1.4	16%	17%	1.8%	2.0%
Average exclude BYD(3)						11.0	9.2	1.6	1.3	17%	18%	1.9%	2.2%

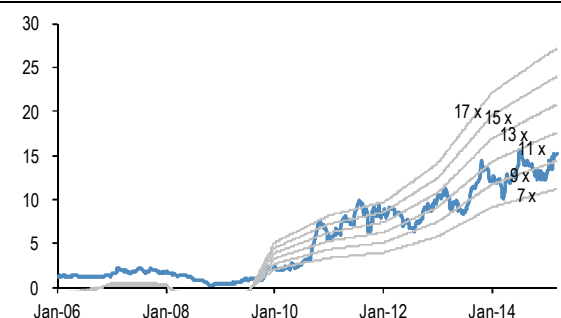
Source: J.P. Morgan estimates, Bloomberg. Notes: (1) Weichai Power is covered by Karen Li. (2) BYD covered by Alvin Kwok. (3) Average P/E is calculated as aggregated sector market cap divided by FY14/15E aggregated sector earnings; averages of P/B, ROE and dividend yield are simple average of the companies listed above.

Valuation and price target basis

We extend our PT to Dec-15 at HK\$19, based on 12x FY15E earnings (vs. a previous June-15 HK\$19 on the same methodology).

Considering Brilliance's historical trading band and growth outlook, we believe 12x is achievable.

Brilliance China forward PE band



Source: Bloomberg, Company data and J.P. Morgan estimates.

JPM vs. consensus, change in estimates

Earnings after minority	FY15E	FY16E
JPM	6,312	7,219
Consensus	5,862	6,898
% Difference	8%	5%

Source: Bloomberg, J.P. Morgan estimates.

Table 1: Brilliance China earnings revisions

RMB mn	2014E			2015E		
	Revised	Previous	Change %	Revised	Previous	Change %
Net Sales	6,033	6,033	0%	6,102	6,102	0%
Sales growth (%)	-1%	-1.2%		1%	1.1%	
COGS	(5,330)	(5,330)	0%	(5,384)	(5,384)	0%
Gross profit	703	703	0%	717	717	0%
Gross margin (%)	12%	12%		12%	11.8%	
Operating profit	(105)	(105)		(100)	(100)	
Operating margin (%)	-2%	-1.7%		-2%	-1.6%	
Pre-tax profit	5,319	5,221	2%	6,408	6,525	-2%
Net profit	5,298	5,117	4%	6,312	6,330	0%
Net margin (%)	88%	85%		103%	104%	
Net profit growth (%)	57%	52%		19%	24%	
EPS (fully diluted)	1.05	1.02	4%	1.26	1.26	0%
EPS growth (%)	57%	52%		19%	24%	

Source: J.P. Morgan.

Table 2: BMW equity accounted investment income

BMW's equity accounted investment income from JVs (Euro mn)					
1Q11	2Q11	3Q11	4Q11	FY11	
49	31	44	38	162	
1Q12	2Q12	3Q12	4Q12	FY12	
43	105	51	72	271	
1Q13	2Q13	3Q13	4Q13	FY13	
87	166	124	30	407	
1Q14	2Q14	3Q14	4Q14	FY14	
225	201	170	59	655	

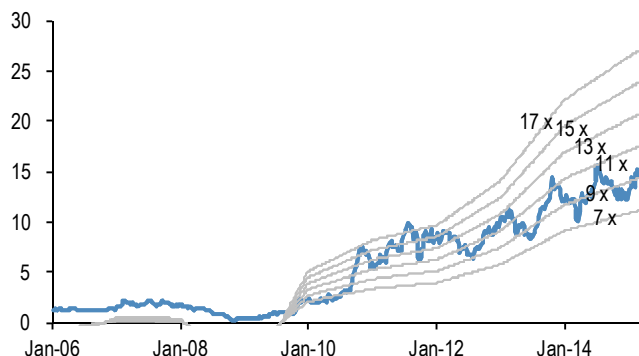
Source: Company. Note: (1) BMW's equity income included three jointly controlled JVs before 2014, including Brilliance China (50-50%) and DriveNow (50-50%) and SGL. Equity income starting FY14 includes only Brilliance BMW and DriveNow. (2) FY13 number has been adjusted due to first-time application of IFRS 10, IFRS 11 and IFRS 12.

Table 3: BMW equity accounted investment income

	Brilliance BMW equity income reported by BMW (Euro mn)	Brilliance BMW net income reported by Brilliance China (Rmb mn)	EURCNY FX rate	Brilliance China's consolidated net income (Rmb mn)
FY11	192	1,720	8.96	1,812
FY12	282	2,325	8.26	2,301
FY13	417	3,435	8.24	3,374
FY14	670	JPM Rmb5.5-5.6bn		JPM Rmb5.3-5.4bn

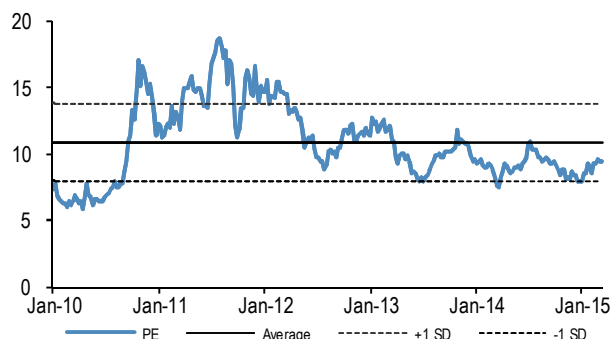
Source: Company data, J.P. Morgan estimates.

Figure 1: Brilliance China forward P/E band



Source: Bloomberg, J.P. Morgan estimates.

Figure 2: Brilliance China forward P/E with +/-1.0 standard deviation



Source: Bloomberg, J.P. Morgan estimates.

Investment Thesis, Valuation and Risks

Brilliance China Automotive (*Overweight; Price Target: HK\$19.00*)

Investment Thesis

We like Brilliance China, given its distinctive position in the premium car market in China. Its expected volume growth of ~20% in 2015/16 is also well above the broader passenger vehicle market based on our forecasts. Following completion of the Tiexi plant expansion in Oct-13 (which is dedicated to manufacturing the BMW 3-series and X1 SUV), we anticipate that strong sequential volume growth from these models should help keep unit costs low and sustain margins even though these models carry lower ASP than the BMW 5-series. We are OW on the stock, and it is one of our preferred picks in the China auto space.

Valuation

We reset our PT to Dec-15 at HK\$19 from Jun-15 PT (HK\$19), based on the same methodology of 12x FY15E earnings. Considering Brilliance's historical trading band and growth outlook, we believe 12x is achievable.

Risks to Rating and Price Target

Risks include worse-than-expected sales volume and higher-than-anticipated expenses in the Brilliance-China JV.

Brilliance China Automotive: Summary of Financials

Income Statement						Cash flow statement					
Rmb in millions, year end Dec	FY12	FY13	FY14E	FY15E	FY16E	Rmb in millions, year end Dec	FY12	FY13	FY14E	FY15E	FY16E
Revenues	5,916	6,103	6,033	6,102	6,099	EBIT	2,533	3,521	5,470	6,561	7,836
% change Y/Y	(8.2%)	3.2%	(1.2%)	1.1%	(0.0%)	Depreciation & amortization	140	139	174	168	154
Gross Profit	696	687	703	717	745	Change in working capital	(133)	4	(370)	(24)	(291)
EBIT	2,533	3,521	5,470	6,561	7,836	Others	(2,304)	(3,622)	(5,446)	(6,604)	(8,213)
% change Y/Y	22.7%	39.0%	55.3%	20.0%	19.4%	Cash flow from operations	(2)	(154)	(323)	(52)	(670)
EBIT Margin	42.8%	57.7%	90.7%	107.5%	128.5%	Capex	(526)	(616)	(600)	(600)	(600)
Net Interest	(174)	(139)	(151)	(154)	(156)	Free cash flow	(355)	(602)	(773)	(500)	(1,118)
Earnings before tax	2,295	3,325	5,319	6,408	7,680	Equity raised/(repaid)	5	0	0	0	0
% change Y/Y	17.7%	44.9%	60.0%	20.5%	19.9%	Debt raised/(repaid)	27	151	147	32	29
Tax	(58)	(8)	(21)	(96)	(461)	Dividends paid	0	(394)	(403)	(424)	(506)
Net income (core)	2,301	3,374	5,298	6,312	7,219	Other	(143)	(7)	0	0	0
% change Y/Y	27.0%	46.6%	57.0%	19.1%	14.4%	Cash flow from financing	(110)	(250)	(255)	(392)	(476)
Shares Outstanding	5,024	5,026	5,026	5,026	5,026	Beginning cash	586	837	903	917	1,185
EPS (core) (Rmb)	0.46	0.67	1.05	1.26	1.44	Ending cash	837	903	917	1,185	881
% change Y/Y	26.3%	46.6%	57.0%	19.1%	14.4%						
Balance sheet						Ratio Analysis					
Rmb in millions, year end Dec	FY12	FY13	FY14E	FY15E	FY16E	Rmb in millions, year end Dec	FY12	FY13	FY14E	FY15E	FY16E
Cash and cash equivalents	1,949	2,117	2,149	2,776	2,065	Net margin	38.9%	55.3%	87.8%	103.4%	118.4%
Accounts receivable	1,812	2,220	2,430	2,455	2,731	Sales growth	(8.2%)	3.2%	(1.2%)	1.1%	(0.0%)
Inventories	838	769	730	738	733	Net profit growth	27.0%	46.6%	57.0%	19.1%	14.4%
Others	1,818	1,418	3,110	8,498	15,767	Sales/assets	0.4	0.3	0.3	0.3	0.2
Current assets	6,417	6,524	8,419	14,467	21,295	Assets/equity	169.8%	152.2%	142.3%	132.9%	124.4%
Net fixed assets	1,745	1,686	1,551	1,422	1,307	ROE	27.1%	29.3%	37.9%	35.4%	29.9%
Intangibles	424	731	731	731	731						
Other LT assets	611	612	612	612	612						
Total Assets	16,058	18,990	20,761	26,690	33,413						
ST loans	1,119	1,528	1,675	1,708	1,737						
Payables	4,828	4,289	4,017	4,026	4,007						
Others	910	975	975	975	975						
Total current liabilities	6,857	6,793	6,668	6,710	6,720						
Long-term debt	0	0	0	0	0						
Other LT liabilities	2	56	56	56	56						
Total non-current liabilities	2	56	56	56	56						
Total Liabilities	6,859	6,849	6,724	6,766	6,776						
Shareholders' equity	10,015	13,015	14,910	20,798	27,511						
Minorities	(816)	(874)	(874)	(874)	(874)						
BVPS	1.99	2.59	2.95	4.14	5.47						

Source: Company reports and J.P. Morgan estimates.

JPM Q-Profile

Brilliance China Automotive Holdings Limited (HONG KONG / Consumer Discretionary)

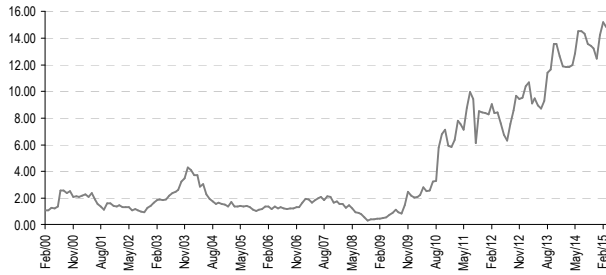
As Of: 13-Mar-2015



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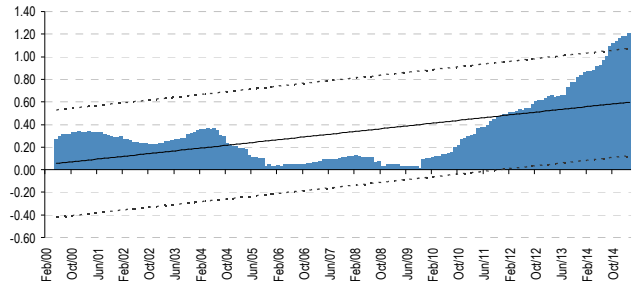
Local Share Price

Current: **14.80**



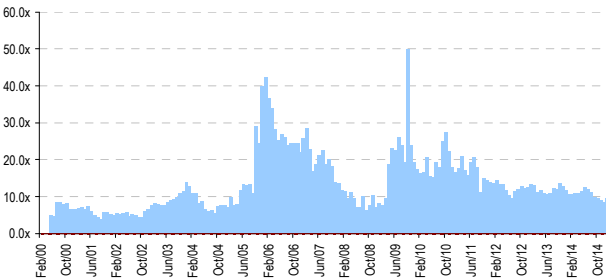
12 Mth Forward EPS

Current: **1.21**



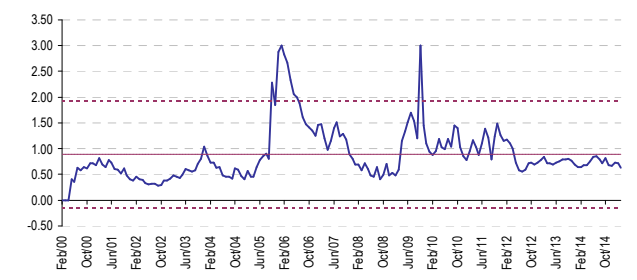
PE (1Yr Forward)

Current: **9.9x**



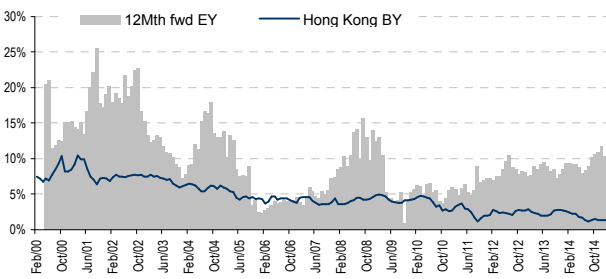
P/E Relative to Hong Kong Index

Current: **0.63**



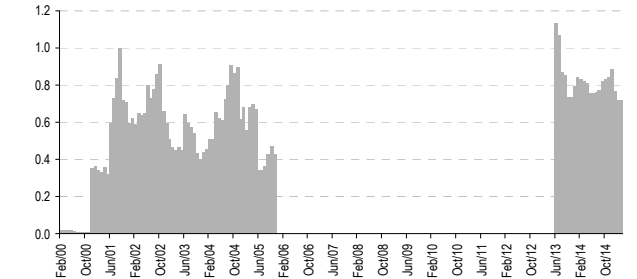
Earnings Yield (& Local Bond Yield)

Current: **10%**



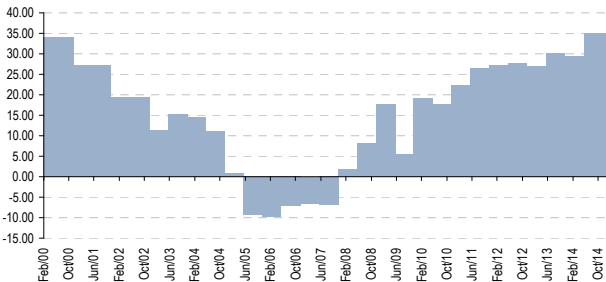
Dividend Yield (Trailing)

Current: **0.72**



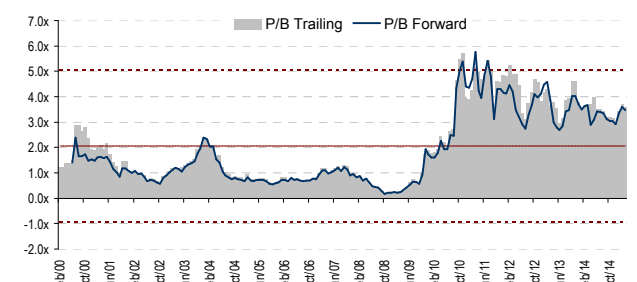
ROE (Trailing)

Current: **35.12**



Price/Book (Value)

Current: **3.6x**



Summary

Brilliance China Automotive Holdings Lir		HONG KONG		TICKER 1114 HK		As Of: 13-Mar-15					
Consumer Discretionary						Local Price: 14.80					
						EPS: 1.21					
	Latest	Min	Max	Median	Average	2 S.D.+	2 S.D. -	% to Min	% to Max	% to Med	% to Avg
12mth Forward PE	9.91x										
P/BV (Trailing)	3.60	0.16	5.75	1.43	2.07	5.08	-0.93	-95%	60%	-60%	-42%
Dividend Yield (Trailing)	0.72x	0.00	1.14	0.01	0.30	0.99	-0.40	-100%	58%	-99%	-59%
ROE (Trailing)	35.12	-9.79	35.12	19.11	15.90	43.87	-12.08	-128%	0%	-46%	-55%

Source: Bloomberg, Reuters Global Fundamentals, IBES CONSENSUS, JPMorgan Quantitative & Derivative Strategy

Other Companies Discussed in This Report (all prices in this report as of market close on 18 March 2015, unless otherwise indicated)

BMW (BMWG.DE/€121.6[17 March 2015]/Overweight), Geely Automobile Holdings Ltd. (0175.HK/HK\$3.60/Overweight)

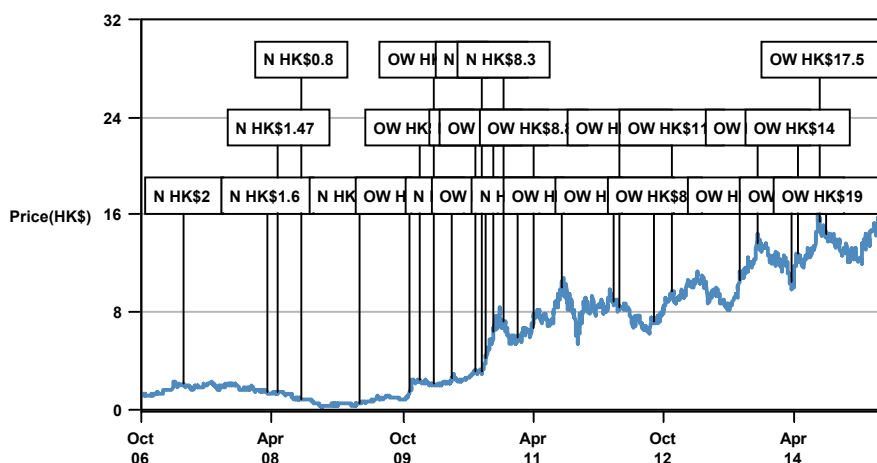
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- **Client:** J.P. Morgan currently has, or had within the past 12 months, the following company(ies) as clients: Geely Automobile Holdings Ltd..
- **Client/Investment Banking:** J.P. Morgan currently has, or had within the past 12 months, the following company(ies) as investment banking clients: Geely Automobile Holdings Ltd..
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Brilliance China Automotive (1114.HK, 1114 HK) Price Chart

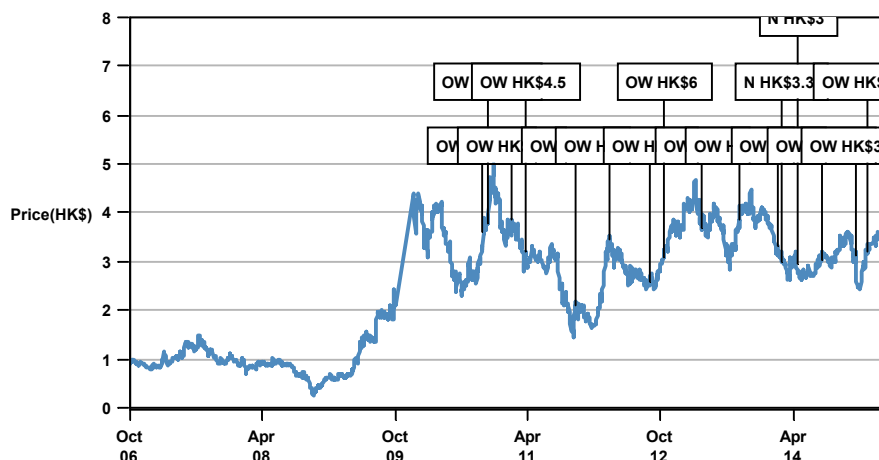


Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Mar 27, 2007.

Date	Rating	Share Price (HK\$)	Price Target (HK\$)
27-Mar-07	N	2.13	2.00
11-Mar-08	N	1.52	1.60
22-Apr-08	N	1.43	1.47
29-Jul-08	N	0.89	0.80
05-Apr-09	N	0.51	0.75
30-Oct-09	OW	1.45	1.80
09-Dec-09	OW	2.46	2.80
03-Feb-10	OW	2.14	2.80
21-Apr-10	N	2.55	2.80
30-Jul-10	N	3.11	3.30
27-Aug-10	N	3.08	3.50
14-Sep-10	OW	4.26	5.20
15-Oct-10	OW	6.42	9.60
26-Nov-10	N	7.17	8.30
28-Jan-11	N	5.87	7.50
29-Mar-11	OW	6.77	8.80
29-Jul-11	OW	9.95	12.50
29-Feb-12	OW	8.93	11.60
29-Mar-12	OW	8.32	11.00
14-Aug-12	OW	7.15	8.00
02-Nov-12	OW	9.62	11.00

13-Aug-13	OW	10.66	13.00
24-Oct-13	OW	13.66	20.00
20-Mar-14	OW	10.50	13.00
15-Apr-14	OW	12.76	14.00
11-Jul-14	OW	15.46	17.50
05-Aug-14	OW	14.40	19.00

Geely Automobile Holdings Ltd. (0175.HK, 175 HK) Price Chart



Date	Rating	Share Price (HK\$)	Price Target (HK\$)
26-Sep-10	OW	3.59	4.30
15-Oct-10	OW	3.79	6.20
28-Jan-11	OW	3.84	5.40
24-Mar-11	OW	3.18	4.50
18-Oct-11	OW	2.11	3.30
29-Feb-12	OW	3.45	5.10
14-Aug-12	OW	2.57	4.00
13-Oct-12	OW	3.09	6.00
21-Mar-13	OW	3.71	7.00
23-Aug-13	OW	3.86	7.50
24-Jan-14	OW	3.32	5.00
14-Feb-14	N	3.01	3.30
15-Apr-14	N	2.94	3.00
24-Jul-14	OW	3.02	3.70
16-Dec-14	OW	3.11	3.50
02-Feb-15	OW	3.19	4.30

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Sep 26, 2010.

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J.P. Morgan Equity Research Ratings Distribution, as of January 1, 2015

	Overweight (buy)	Neutral (hold)	Underweight (sell)
J.P. Morgan Global Equity Research Coverage	45%	43%	12%
IB clients*	56%	49%	33%
JPMS Equity Research Coverage	45%	48%	7%
IB clients*	75%	67%	52%

*Percentage of investment banking clients in each rating category.

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Asia Pacific Equity Research
18 March 2015

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