

Equities

Hong Kong/China

Company Update

Company Report

Geely Auto (175 HK)

19 March 2015

Decline in 2H Gross Margin Offset by Better Sales Mix

Geely Auto's 2014 earnings was down 46% y/y to Rmb1,431m, which is below consensus estimate by 4% (or 8% above our estimate). If we look at 2H14 only, earnings actually fell 75% y/y to only Rmb317m, mainly due to the forex loss that arises from the devaluation of the Ruble in its Russian operation which amounts to Rmb648m. In the end it is not surprising because a profit warning has been issued back in December.

- 2014 sales volume down 24%.** Geely sold a total of 417,851 units of vehicles in 2014, down 24% y/y and 14.3% of which or 59,721 units were sold overseas, down 50% from last year. Despite the decline, export volume still accounts for 11.2% of the total export of China's passenger vehicles (source: CAAM). That makes Geely one of the leading vehicle exporters in China.
- More visible product line.** Upon completion of restructuring last year, Geely has a more visible product line for the next two years. Besides GC9 which is launched this month, the company will roll out an Emgrand electric vehicle by mid-2015, as well as a new Emgrand SUV and compact SUV by end of 2015. In early 2016, an Emgrand cross vehicle and Emgrand 4-door sedan will reach the market, too.
- Raise target price to HK\$4.0.** Since 2H14 sales volume and gross margin are not as low as we expected, we raise our 2015 earnings by 9% to reflect a 3% increase in our sales volume assumption, higher ASP and gross margin, which are offset by a higher tax rate of 25%. We maintain our Accumulate rating and our new target price of HK\$4.0 reflects the same target PE multiple of 12x.

Investment Summary

FY-end Dec	2013	2014	2015E	2016E	2017E
Turnover (Rmb m)	28,708	21,738	23,488	25,140	26,908
Growth (%)	16.6	(24.3)	8.0	7.0	7.0
Net Profit (Rmb m)	2,663	1,431	2,318	2,603	2,834
Growth (%)	30.5	(46.3)	62.0	12.3	8.9
EPS (RMB)	0.30	0.16	0.26	0.30	0.32
Growth (%)	15.5	(46.6)	62.0	12.3	8.9
PER (x)	9.2	17.3	10.7	9.5	8.7
OCF/Share (Rmb)	0.40	0.23	0.45	0.79	0.36
P/B (x)	1.5	1.4	1.3	1.1	1.0
EV/EBITDA (x)	4.3	7.2	4.5	3.1	2.6
DPS (Rmb)	0.04	0.02	0.03	0.04	0.04
Yield (%)	1.4	0.7	1.2	1.3	1.4

Source: Company data, CER estimates

China / Automobile

ACCUMULATE

Share Price	Target Price	Upside
HK\$3.6	HK\$4.0	11.1%

(as of 18 March 2015)

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52 Range (HK\$)	2.4-3.68
DVD yield %	1.27

Latest Key Data

FF no of shares (m)	4,979
FF (%)	56.57
FF market cap (HK\$ m)	17,925
12M daily turnover (HK\$ m)	132.94
12M volatility (%)	36.80
12M Hi/Lo (HK\$)	2.4-3.68
PEG FY15-17E (x)	1.0
RoAE FY14 (%)	8.6
P/B FY15E (x)	1.3
Net debt/equity FY14 (%)	Net cash

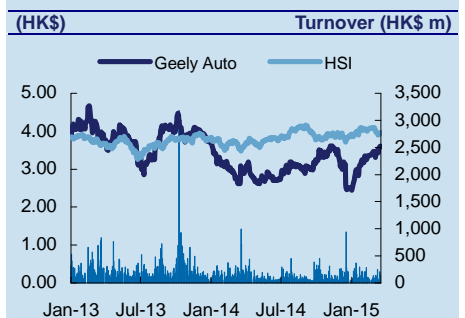
Performance (%)

	1M	YTD	12M
Absolute	7.1	45.7	16.5
Relative to HSCEI	7.8	45.8	(11.6)

Major Shareholders (%)

Proper Glory Holding	27.98
Zhejiang Geely Merrie	8.82

Price Chart



Source: Bloomberg, CER estimates

- **Better sales mix.** In 2H14, sales was down 16% y/y due to weak sales and gross margin declined by nearly 4%-pt to 16.4%, which was not as bad as we expected. Another positive is that there are more high-priced models in the mix and so the higher ASP can more than offset the discounts offered to domestic dealers.
- **Export could continue to face challenge in 2015.** For the export market, PV demand in Russia has stabilized but frequent regulatory changes, weakening currencies and political uncertainties could affect sales. Also, change in tax laws in Brazil, Ukraine and Russia could add further uncertainties to overseas sales in 2015.
- **Strong financial position.** A final dividend of HK\$2.5 cents was issued, with payout ratio staying at 12%. The company has a net cash of Rmb4.7bn and will continue to invest in R&D and make acquisitions this year.

Table: P&L summary for Geely Auto

Year end Dec 31	2013	2014	1H13	2H13	1H14	2H14
Rmb m						
Revenue	28,708	21,738	14,855	13,853	10,158	11,580
+/-	17%	-24%	33%	3%	-32%	-16%
Cost of sales	(22,942)	(17,776)	(12,008)	(10,934)	(8,092)	(9,683)
Gross profit	5,766	3,963	2,847	2,919	2,066	1,897
+/-	26%	-31%	47%	11%	-27%	-35%
Gross margin	20.1%	18.2%	19.2%	21.1%	20.3%	16.4%
Other income	1,062	1,055	552	510	554	500
Distribution and selling expenses	(1,705)	(1,250)	(821)	(884)	(557)	(694)
Admin expenses	(1,682)	(1,772)	(747)	(935)	(599)	(1,173)
SG&A per sales	11.8%	13.9%	10.6%	13.1%	11.4%	16.1%
Share-based payments	(87)	(60)	(46)	(41)	(31)	(29)
Operating profit	3,354	1,935	1,785	1,568	1,434	501
+/-	23%	-42%	31%	15%	-20%	-68%
Operating margin	11.7%	8.9%	12.0%	11.3%	14.1%	4.3%
Finance costs, net	(40)	(24)	(57)	17	(3)	(21)
Share of results of associates and JV	(10)	32	0	(10)	2	30
Profit before taxation	3,304	1,943	1,725	1,579	1,433	510
Taxation	(624)	(494)	(323)	(301)	(307)	(187)
Effective tax rate	18.9%	25.4%	18.7%	19.1%	21.4%	36.6%
Non-controlling interests	(17)	(19)	(3)	(14)	(12)	(6)
as % of post-tax profit	0.6%	0.8%	0.2%	1.1%	1.1%	2.0%
Net profit to shareholders' equity	2,663	1,431	1,398	1,265	1,113	317
+/-	30.5%	-46.3%	37%	24%	-20%	-75%
Net margin	9.3%	6.6%	9.4%	9.1%	11.0%	2.7%
As % of FY	100.0%	100.0%	52.5%	47.5%	77.8%	22.2%

Source: Company data and CER estimates

COMPANY DESCRIPTION

Geely Automobile Holdings is an automobile manufacturer, focusing on development, manufacturing and sales of passenger vehicles. Headquartered in Hangzhou, it has nine manufacturing plants in Linhai, Ningbo, Luqiao, Shanghai, Lanzhou, Xiangtan, Jinan, Chengdu and Cixi in China, and a total annual production capacity of 625,000 units per shift by end of 2012. Geely sells its 14 major sedan models, powered by its own 1.0L-2.4L petro-engines and branded under GLEagle, Emgrand and Englon.

Profit & Loss (Consolidated)

FY-end 31 Dec (Rmb m)	2013	2014	2015E	2016E	2017E
Sales	28,708	21,738	23,488	25,140	26,908
Cost of sales	(22,942)	(17,776)	(18,908)	(20,112)	(21,526)
Gross profit	5,766	3,963	4,580	5,028	5,382
Other income	1,062	1,055	1,174	1,257	1,345
Operating expenses	(1,705)	(1,250)	(1,292)	(1,383)	(1,480)
Operating profit	3,354	1,935	3,158	3,510	3,761
Finance cost, net	(40)	(24)	(22)	(12)	48
Share of P/L of assoc. & JCE	(10)	32	(20)	0	0
Pre-tax profit	3,304	1,943	3,116	3,498	3,809
Tax	(624)	(494)	(779)	(875)	(952)
Minorities	(17)	(19)	(19)	(21)	(23)
Net profit	2,663	1,431	2,318	2,603	2,834
EBITDA	4,432	2,808	4,368	4,825	5,181
EBIT	3,354	1,935	3,158	3,510	3,761
EPS (Rmb)	0.30	0.16	0.26	0.30	0.32
DPS (Rmb)	0.04	0.02	0.03	0.04	0.04

Source: Company, CER estimates

Cash Flow (Consolidated)

FY-end 31 Dec (Rmb m)	2013	2014	2015E	2016E	2017E
Operating cash flow	3,562	2,033	3,959	6,960	3,152
Net profit	2,663	1,431	2,318	2,603	2,834
Depreciation & amortization	(1,078)	(874)	(1,210)	(1,315)	(1,420)
Change in working capital	(449)	(960)	348	2,988	(1,099)
Others	2,425	2,436	2,503	2,685	2,837
Investment cash flow	(865)	(1,468)	(3,219)	(1,543)	(1,545)
Net Capex	(103)	(436)	(1,000)	(1,000)	(1,000)
Disposal	610	24	0	0	0
Change in LT investment	(548)	(16)	0	0	0
Change in other assets	(824)	(1,039)	(2,219)	(543)	(545)
Free cash flow	2,696	565	740	5,418	1,607
Financing cash flow	(1,366)	1,172	(512)	(537)	(506)
Change in share capital	11	0	0	0	0
Net change in debt	(930)	(274)	(200)	(200)	(200)
Dividend paid	(264)	(320)	(290)	(325)	(354)
Net impact of exchange	(41)	(12)	0	0	0
Net cash flow	1,330	1,737	228	4,881	1,101

Source: Company, CER estimates

Balance Sheet (Consolidated)

FY-end 31 Dec (Rmb m)	2013	2014	2015E	2016E	2017E
Total assets	33,599	37,280	36,156	40,961	42,683
Current assets	22,251	25,303	22,240	26,861	28,502
Cash & ST investments	5,583	7,251	7,479	12,359	13,460
Marketable securities & ST inv	13	15	15	15	15
Account & notes receivable	14,785	16,385	13,216	12,957	13,287
Inventories	1,784	1,620	1,489	1,487	1,698
Others	86	32	42	42	42
Non-current assets	11,348	11,977	13,916	14,101	14,181
LT investments	688	719	719	719	719
Net fixed assets	6,209	5,861	7,445	7,571	7,626
Others	4,452	5,397	5,752	5,811	5,836
Total liabilities	17,370	19,814	16,661	19,190	18,431
Current liabilities	17,237	17,845	14,693	17,221	16,463
Account payable	16,075	17,017	14,064	16,792	16,234
ST borrowings	966	692	492	292	92
Others	197	137	137	137	137
Non-current liabilities	133	1,969	1,969	1,969	1,969
Long-term debts	0	0	0	0	0
Others	133	1,969	1,969	1,969	1,969
Total equities	16,230	17,466	19,495	21,772	24,251
Shareholders' equity	16,068	17,288	19,316	21,594	24,073
Minority shareholders	162	178	178	178	178
Total liabilities + SH equities	33,599	37,280	36,156	40,961	42,683
Net cash / (debt)	4,512	4,691	5,120	10,200	11,501
Working capital	494	988	640	(2,348)	(1,249)
Total capital employed	17,195	19,978	21,806	23,884	26,163
Shareholders' equity + Minorities	16,230	17,466	19,495	21,772	24,251
Net gearing (%)	(28.1)	(27.1)	(26.5)	(47.2)	(47.8)

Source: Company, CER estimates

Financial Summary

FY-end 31 Dec	2013	2014	2015E	2016E	2017E
Growth (%)					
Revenue	16.6	-24.3	8.0	7.0	7.0
EBITDA	23.6	-36.6	55.5	10.5	7.4
EBIT	23.1	-42.3	63.2	11.1	7.2
Net profit	30.5	-46.3	62.0	12.3	8.9
EPS	15.5	-46.6	62.0	12.3	8.9
Margins (%)					
Gross	20.1	18.2	19.5	20.0	20.0
EBITDA	15.4	12.9	18.6	19.2	19.3
EBIT	11.7	8.9	13.4	14.0	14.0
Net	9.3	6.6	9.9	10.4	10.5
Others (%)					
Effective tax rate	18.9	25.4	25.0	25.0	25.0
Payout ratio	12.0	12.2	12.5	12.5	12.5
RoCE	16.6	8.3	12.0	12.1	11.8
Average RoE	18.4	8.6	12.7	12.7	12.4
Average RoA	8.2	4.0	6.3	6.7	6.8
Interest cover (x)	84	82	142	300	-79

Source: Company, CER estimates

Everbright Research Limited Rating System

Buy	Expected to outperform the benchmark index by >15% over the next six months
Accumulate	Expected to outperform the benchmark index by 5 - 15% over the next six months
Hold	Expected to outperform or underperform the benchmark index by <5% over the next six months
Reduce	Expected to underperform the benchmark index by 5 - 15% over the next six months
Sell	Expected to underperform the benchmark index by >15% over the next six months

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