

JPM-pp1

Asia Pacific Equity Research

22 March 2015

Great Wall Motor - H (2333 HK)

Overweight

Price: HK\$49.30

20 Mar 2015

Price Target: HK\$60.00

PT End Date: 30 Dec 2015

Management's SUV endeavours

GWM's management hosted a conference call and conveyed to investors the company's long-term strategy in China. We are OW on GMW with a Dec-15 PT of HKD60. We summarize key takeaways from the conference call.

FY14 results and FY15 outlook

- **Margins** in 4Q14 were lower due to new model launches and year-end bonuses. Bonus expense in FY14 was higher than FY13 as the company had a total of 70k employees by end-14 vs 60k by end-13. Management believes margins in FY15 would improve due to better product mix.
- **Margin by model:** H6 gross margin in FY14 was similar to FY13 (>30%) despite the company lowering H6's MSRP by Rmb6k in Sep (upgrade version only). H2 gross margin is lower than H6 and H1's gross margin is similar to the sedan.
- **Sales target** of 850k units (16% YoY growth) in FY15 is a conservative expectation, according to management, and all of the incremental volumes will come from SUVs.
- **Cash** at the end of 2014 dropped to Rmb3bn vs FY13 at Rmb5.5bn mainly due to increases in A/R. As 95% of the company's dealers purchase vehicles with bank notes (usually on the term of six months), a big portion of the bank notes issued in 4Q14 had not been translated into cash by end-14. These bank notes are expected to turn into cash in 1H15.
- **Inventory** level of the major models remains very healthy. H6 and H2's inventory days were 10-15 days before Chinese New Year this year and are now at around 20 days. Pickup/sedan inventory days remain around one month at OEM.
- **R&D expense** increased to 4.1% of revenue vs 3% in FY13 due to one-off expenses relating H8. Excluding this one-off item, R&D expense increased by only Rmb200-300mn in FY14 and management expects FY15 normalized capex to increase by 10-20%.
- **Auto financing** penetration rate is around 10% for GWM in the past. GWM established a new auto finance JV in 2H14.

Model launch pipeline

- **H8** will be launched during the Shanghai Auto show in April (nationwide launch). Management expects monthly sales to top 4-5k units initially after production ramp-up.
- **Coupe C** (MSRP Rmb130-160k) will be launched in 2Q15 and **H7** (MSRP Rmb160-190k) in 2H15.
- **AT** (automatic transmission) versions of H6 and H2 will be launched in 2Q15. MSRP of AT versions will be higher than the existing MT versions.
- **Hybrid** version of H7 will be launched between 2H16 and 1H17.
- One additional SUV model produced in Xushi phase 1 will be launched in 2016.

Table 1: Great Wall Motor SUV series and model launch pipeline

	M2	M4	H1	H2	H5
	http://www.gwm.com.cn/Upload/2013/0626/945399_08_15000	http://www.gwm.com.cn/Upload/2014/0704/945399_08_15000			
MSRP (Rmb)	67.9-77.9k	63.9-73.9k	68.9-82.9k	98.8-112.8k	92.8-170.8k
Size (L × W × H mm)	4011 × 1744 × 1735	3995 × 1728 × 1617	3898 × 1729 × 1621	4335 × 1814 × 1695	4650 × 1800 × 1745
Model launch			Launched in Oct 2014	Launched in July 2014; AT version in 2Q15	
	H6	H7	H8	H9	Coupe C
	https://encrypted-tbn1.gstatic.com/images?q=tbn:ANd9GcQSi6LJLj				
MSRP (Rmb)	115.8-162.8k	Estimated 160-190k	201.8-236.8	229.8-272.8k	Estimated 130-160k
Size (L × W × H mm)	4640 × 1825 × 1690 4649×1852×1710 ⁽¹⁾	4677 × 1911 × 1702	4806 × 1975 × 1794	4856 × 1926 × 1900	4545 × 1835 × 1700
Model launch	AT version in 2Q15	2H15; hybrid version in 2H16-1H17	Apr 2015	Launched in Nov 2014	2Q15

Source: Company data, some photos taken by J.P. Morgan at the 2014 Beijing Auto Show. Notes: (1) Sport version

Capacity

- Tianjin phase 2 monthly capacity is 50k units (H2: 15k units, H6: 35k units) based on double shifts. Great Wall might be able to increase Tianjin phase 2 capacity by adding one additional shift but this will potentially lower overall efficiency. Further capacity upside at Tianjin phase 2 might be limited.

Table 2: Great Wall Motor's production plants and capacity

	Baoding I	Baoding II	Baoding III	Tianjin Phase 1	Tianjin Phase 2	Xushi Phase 1	Xushi Phase 2
Designed capacity (unit/year)	200k	100k	100k	250k	250k	250k	250k
Construction complete				Aug 2012	July 2013	Nov 2013	July 2015
Models produced	C20, C30,	H5, pickup trucks	H1, M-series	H6	C50, H2, H6	H8, H9, Coupe C	H7

Source: Company data

Investment Thesis

We maintain our OW on Great Wall Motor-H. The key reasons behind our bullish investment thesis include: (1) we expect GWM to deliver 25%/15% sales volume growth in FY15/16 despite our view that the overall PV market will likely decelerate; (2) GWM is launching six new models in 2H14-2015. For any OEM globally, it is an aggressive proposition. While new model launches will incur higher marketing expenses and production ramp-up costs, GWM's share price historically exhibits a ~90% correlation with concurrent monthly SUV sales, rather than margins; and (3) consensus expectations on sales or earnings are subject to upside risk, in our view.

Valuation

Our PT of HK\$60 (Dec-15) is based on a 13x forward P/E. With the re-launch of the H8 SUV and the coming "killer" model *Coupe C* in 2Q15, we believe GWM is set to see another round of re-rating and share price rally. GWM's P/E multiple has historically been 9-14x; the stock was re-rated during 2009-10 and 2012-13.

Risks to Rating and Price Target

Downside risks include worse-than-expected competition in the SUV business, leading to price competition and margin contraction, and model launch delays. Key power train technology is another longer-term challenge facing the company.

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Date	Rating	Share Price (HK\$)	Price Target (HK\$)
26-Jan-07	OW	9.13	6.20
16-Oct-07	OW	11.40	8.32
12-Mar-08	OW	8.01	6.56
25-Jul-08	OW	5.10	3.76
05-Sep-08	OW	1.38	3.04
02-Dec-08	OW	0.93	1.56
19-Apr-09	OW	1.68	2.12
25-May-09	OW	2.48	3.32
12-Aug-09	OW	3.03	3.52
25-Aug-09	N	2.99	3.52
09-Dec-09	N	3.78	3.64
03-Feb-10	N	4.50	4.40
17-Mar-10	OW	5.49	6.84
21-Apr-10	N	5.97	6.24
30-Jul-10	N	6.27	6.72
21-Aug-10	N	6.32	7.52
15-Oct-10	N	7.94	9.50
28-Jan-11	N	12.12	10.90
02-Aug-11	N	12.14	12.70
18-Oct-11	N	10.22	10.80
29-Feb-12	N	15.06	12.80
14-Aug-12	OW	17.54	20.00
13-Oct-12	OW	21.75	24.00
09-Jan-13	OW	26.30	32.00
21-Mar-13	OW	28.40	37.00
19-Apr-13	OW	28.40	40.00
23-Jul-13	OW	36.15	46.00
14-Oct-13	OW	45.85	65.00
24-Jan-14	OW	36.10	50.00
14-Feb-14	OW	37.25	46.00
15-Apr-14	N	41.55	41.00
10-May-14	N	32.80	25.00
25-Aug-14	N	32.00	35.00
24-Oct-14	OW	32.50	40.00
02-Dec-14	OW	38.10	50.00
21-Mar-15	OW	49.30	60.00

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