



Rating
Buy

Asia
China

Automobiles &
Components

Company
Brilliance China

Reuters 1114.HK	Bloomberg 1114 HK	Exchange HKG	Ticker 1114
ADR Ticker BCAUY	ISIN US10949Q2049		

Date
27 March 2015

Forecast Change

Price at 26 Mar 2015 (HKD)	14.24
Price target - 12mth (HKD)	17.20
52-week range (HKD)	16.06 - 10.42
HANG SENG INDEX	24,497

Strong FY14; outlook still decent w/ new models in FY15E and beyond

Lower 2H14 margin not surprising; new models and engine plant will help

Brilliance's 60% FY14 net profit YoY growth and the 7.3ppt BMW JV 2H14 HoH net profit margin erosion are slightly better than our expectations, considering Brilliance's cautious guidance at the 1H14 results briefing. For FY15-16E, we remain optimistic on Brilliance BMW's growth prospects due to its two to three new model launches, which will drive sales, and due to the opening of the engine manufacturing plant, which should lower costs; maintaining Buy.

2H14 margin squeeze on R&D and marketing, but FY14 margin still improves

Brilliance recorded FY14 net profit of RMB5.4bn (up 60% YoY). A decline in minibus sales volume and mix deterioration led to a 42% YoY widening of the consolidated business operating loss to RMB320.1m. Meanwhile, Brilliance BMW JV recorded 61% FY14 net profit growth YoY on a 35% volume increase and a 2.3ppt YoY net profit margin improvement on enhancing economies of scale. On a HoH basis, the JV reported a 7.3ppt net profit margin decline, as Brilliance BMW booked greater R&D and marketing expenses in 2H.

New models to drive sales; new engine plant to enhance localization

Despite a lack of new models, Brilliance BMW JV delivered 14% YoY growth in January-February wholesale volume. For FY15-16E, we remain optimistic that the addition of production of the 2-series Active Tourer in 2H15E, the new generation X1 SUV, and maybe one extra new model in FY16E (1-series sedan) will enlarge the JV's customer base and allow it to sustain high-teen volume growth. From a margin perspective, we believe the increasing component localization, especially in FY16E with the new engine plant, and the EUR depreciation, will help Brilliance mitigate the margin pressure due to the sales mix downshift and possible R&D expenses on new product localization.

Premium P/E-based target price justified by strong FY15-17E growth; risks

We raise our FY15-16 forecasts to factor in higher margins for the BMW JV. With a 13% FY14-17E three-year EPS CAGR, we still value the stock at a premium 11.5x FY15E P/E; the implied P/E-to-growth ratio of 0.9x does not look demanding. Downside risk: luxury car sales slowdown in China.

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Key changes

Price target	16.30 to 17.20	↑	5.5%
Sales (FYE)	6,357 to 6,307	↓	-0.8%
Op prof margin (FYE)	-5.8 to -4.9	↑	-16.8%
Net profit (FYE)	5,640.9 to 6,029.6	↑	6.9%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	-5.4	15.8	37.5
HANG SENG INDEX	-1.6	4.9	11.9

Source: Deutsche Bank

Forecasts And Ratios

Year End Dec 31	2013A	2014A	2015E	2016E	2017E
Sales (CNYm)	6,103.5	5,514.8	6,307.0	6,860.2	7,390.4
Reported NPAT (CNYm)	3,374.2	5,403.4	6,029.6	6,848.9	7,854.6
DB EPS FD (CNY)	0.67	1.07	1.19	1.35	1.55
OLD DB EPS FD (CNY)	0.67	0.97	1.11	1.27	-
% Change	0.0%	10.4%	6.9%	6.2%	-
DB EPS growth (%)	46.6	60.1	10.9	13.6	14.7
PER (x)	12.8	9.6	9.6	8.5	7.4
Yield (net) (%)	0.9	0.8	1.3	1.4	1.6

Source: Deutsche Bank estimates, company data

¹ DB EPS is fully diluted and excludes non-recurring items

² Multiples and yields calculations use average historical prices for past years and spot prices for current and future years, except P/B which uses the year end close

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Model updated: 26 March 2015

Running the numbers

Asia
China
Automobiles & Components

Brilliance China

Reuters: 1114.HK Bloomberg: 1114.HK

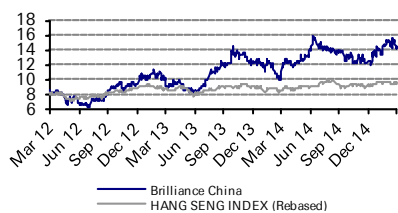
Buy

Price (26 Mar 15) HKD 14.24
Target Price HKD 17.20
52 Week range HKD 10.42 - 16.06
Market Cap (m) HKDm 71,567
USDm 9,229

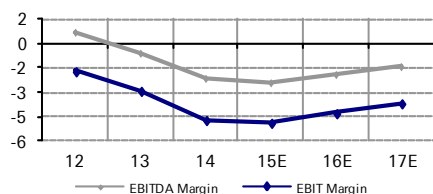
Company Profile

Brilliance China Automotive Holdings Limited, through its subsidiaries and JVs, manufactures and distributes minibuses and sedans in the People's Republic of China. The company also manufactures and trades automotive components.

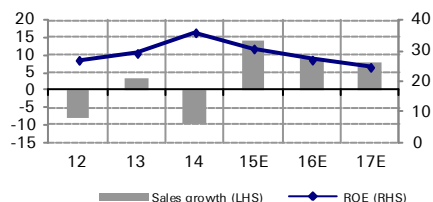
Price Performance



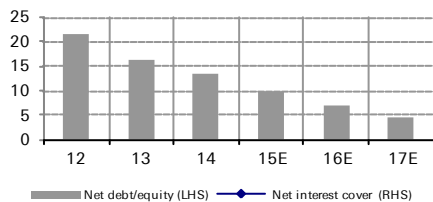
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 31-Dec

Financial Summary

	2012	2013	2014	2015E	2016E	2017E
DB EPS (CNY)	0.46	0.67	1.07	1.19	1.35	1.55
Reported EPS (CNY)	0.46	0.67	1.07	1.19	1.35	1.55
DPS (CNY)	0.00	0.08	0.09	0.14	0.16	0.19
BVPS (CNY)	2.0	2.6	3.4	4.4	5.6	7.0
Weighted average shares (m)	5,024	5,026	5,026	5,026	5,026	5,026
Average market cap (CNYm)	33,450	42,860	51,579	57,346	57,346	57,346
Enterprise value (CNYm)	26,043	32,702	37,571	38,271	32,527	25,901

Valuation Metrics

P/E (DB) (x)	14.6	12.8	9.6	9.6	8.5	7.4
P/E (Reported) (x)	14.6	12.8	9.6	9.6	8.5	7.4
P/BV (x)	3.89	3.87	2.94	2.58	2.03	1.63
FCF Yield (%)	nm	nm	nm	nm	nm	nm
Dividend Yield (%)	0.0	0.9	0.8	1.3	1.4	1.6
EV/Sales (x)	4.4	5.4	6.8	6.1	4.7	3.5
EV/EBITDA (x)	654.1	nm	nm	nm	nm	nm
EV/EBIT (x)	nm	nm	nm	nm	nm	nm

Income Statement (CNYm)

Sales revenue	5,916	6,103	5,515	6,307	6,860	7,390
Gross profit	836	826	702	752	847	940
EBITDA	40	-38	-119	-154	-132	-107
Depreciation	101	102	110	122	128	130
Amortisation	39	37	30	31	33	34
EBIT	-100	-177	-259	-307	-293	-271
Net interest income/(expense)	-100	-92	-103	-126	-146	-166
Associates/affiliates	2,526	3,641	5,766	6,364	7,189	8,193
Exceptionals/extraordinaries	-31	-48	-61	0	0	0
Other pre-tax income/(expense)	0	0	0	0	0	0
Profit before tax	2,295	3,325	5,343	5,932	6,750	7,756
Income tax expense	58	8	43	11	11	11
Minorities	-64	-58	-103	-109	-110	-110
Other post-tax income/(expense)	0	0	0	0	0	0
Net profit	2,301	3,374	5,403	6,030	6,849	7,855
DB adjustments (including dilution)	0	0	0	0	0	0
DB Net profit	2,301	3,374	5,403	6,030	6,849	7,855

Cash Flow (CNYm)

Cash flow from operations	-2	-154	211	-182	-233	-234
Net Capex	-465	-586	-500	-500	-500	-500
Free cash flow	-467	-740	-289	-682	-733	-734
Equity raised/(bought back)	5	0	-1,050	0	0	0
Dividends paid	0	-394	-437	-724	-822	-943
Net inc/(dec) in borrowings	27	151	459	334	297	282
Other investing/financing cash flows	685	1,050	1,308	1,524	1,726	1,974
Net cash flow	251	67	-10	452	469	579
Change in working capital	236	-2	537	108	57	49

Balance Sheet (CNYm)

Cash and other liquid assets	837	903	1,179	1,631	2,099	2,679
Tangible fixed assets	1,808	1,747	2,020	2,398	2,769	3,140
Goodwill/intangible assets	362	670	996	965	932	898
Associates/investments	8,583	11,263	15,194	20,034	25,497	31,716
Other assets	4,468	4,407	3,819	4,268	4,601	4,925
Total assets	16,058	18,990	23,207	29,296	35,898	43,356
Interest bearing debt	2,829	2,883	3,342	3,676	3,973	4,255
Other liabilities	4,030	3,966	3,911	4,468	4,857	5,230
Total liabilities	6,859	6,849	7,253	8,145	8,830	9,486
Shareholders' equity	10,015	13,015	16,931	22,237	28,264	35,176
Minorities	-816	-874	-977	-1,086	-1,196	-1,306
Total shareholders' equity	9,198	12,141	15,954	21,151	27,068	33,870
Net debt	1,993	1,980	2,163	2,045	1,874	1,577

Key Company Metrics

Sales growth (%)	-8.2	3.2	-9.6	14.4	8.8	7.7
DB EPS growth (%)	23.4	46.6	60.1	10.9	13.6	14.7
EBITDA Margin (%)	0.7	-0.6	-2.2	-2.4	-1.9	-1.4
EBIT Margin (%)	-1.7	-2.9	-4.7	-4.9	-4.3	-3.7
Payout ratio (%)	0.0	11.7	8.1	12.0	12.0	12.0
ROE (%)	27.1	29.3	36.1	30.8	27.1	24.8
Capex/sales (%)	8.9	10.1	9.1	7.9	7.3	6.8
Capex/depreciation (x)	3.8	4.4	3.6	3.3	3.1	3.0
Net debt/equity (%)	21.7	16.3	13.6	9.7	6.9	4.7
Net interest cover (x)	nm	nm	nm	nm	nm	nm

Source: Company data, Deutsche Bank estimates

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FY14 results snapshot

Year-end cost spike cannot mask strong full-year results

Brilliance's minibus/auto parts business reported a 9.6% YoY revenue decline, to RMB5.5bn, and an 18.1% YoY gross profit decline, to RMB562.5m, due to weaker mix and pricing. According to management, its minibus sales were affected by weak overall market demand and a lack of new models. Partially offset by government grants, lower transportation expenses, and lower advertising expenses, the consolidated business still recorded a 42.2% larger operating loss of RMB320.1m YoY in FY14.

Not surprisingly, Brilliance's FY14 bottom line was lifted up by the BMW JV, which reported 29.2% YoY growth in revenues and a 61.2% YoY jump in earnings contributions (RMB5.5bn). There was margin expansion at the BMW JV, despite a product mix downshift, due to economies of scale and increasing component localization. On a half-year basis, the JV recorded greater R&D and selling expenses in 2H14. That led to 7.3ppt HoH 2H14 net profit margin erosion, but we do not find that surprising, as Brilliance has been warning of lower margins in 2H due to cost allocation seasonality and because a similar situation took place in previous years.

Figure 1: Brilliance China – FY14 results summary

RMBm	FY14	FY13	YoY	2H14	1H14	HoH	DB Comments (FY14 vs. FY13)
Turnover	5,514.8	6,103.5	-9.6%	3,018.9	2,495.9	21.0%	FY14: Minibus sales volume sales dropped 7.2% to 77,710 units (from FY13's 83,747 units)
Cost of sales	(4,952.3)	(5,417.0)	-8.6%	(2,674.1)	(2,278.2)	17.4%	
Gross profit	562.5	686.5	-18.1%	344.7	217.7	58.3%	
<i>Gross profit margin</i>	<i>10.2%</i>	<i>11.2%</i>		<i>11.4%</i>	<i>8.7%</i>		Margin was negatively affected primarily due to volume decline, sales mix change, and pricing pressure
Other net income	104.2	96.2	8.3%	77.1	27.1	183.9%	Including government grants, which were partially offset by a decrease in income generated from the sale of scrap materials
Selling expenses	(585.2)	(608.4)	-3.8%	(354.7)	(230.5)	53.9%	Decrease in transportation cost as a result of lower sales volume and lower advertising spending
General & admin expenses	(401.6)	(399.4)	0.5%	(213.7)	(187.9)	13.7%	
Operating profit/(losses)	(320.1)	(225.0)	42.2%	(146.6)	(173.5)	-15.5%	
<i>Operating profit margin</i>	<i>-5.8%</i>	<i>-3.7%</i>		<i>-4.9%</i>	<i>-6.9%</i>		
Net interest income (expenses)	(102.7)	(91.7)	12.0%	(49.4)	(53.3)	-7.4%	Due to increase in borrowing, partially offset by increase in interest income due to increase in cash deposit
Share of associates' profit	228.9	193.1	18.5%	106.5	122.4	-12.9%	Including contributions from The Aerospace Mitsubishi engine and Power Xincheng
Share of JV's profit	5,536.8	3,448.3	60.6%	1,847.5	3,689.2	-49.9%	The BMW JV had a 34.7% YoY sales volume growth to 278,529 units. Earnings contribution was up 61.2% YoY to RMB5.5bn.
Profit before taxation	5,342.9	3,324.7	60.7%	1,758.1	3,584.8	-51.0%	
Taxation	(42.9)	(8.4)	412.7%	(37.6)	(5.3)	607.1%	Due to the dividend withholding tax and an effective tax rate increase for one of the company's subsidiary
Minority interests	103.5	57.8	78.9%	55.0	48.4	13.6%	
Net profit	5,403.4	3,374.2	60.1%	1,775.5	3,627.9	-51.1%	

Source: Company data, Deutsche Bank estimates



New product cycle in sight

BMW JV

Existing model sales to stay solid, with new model support beyond 2H15E

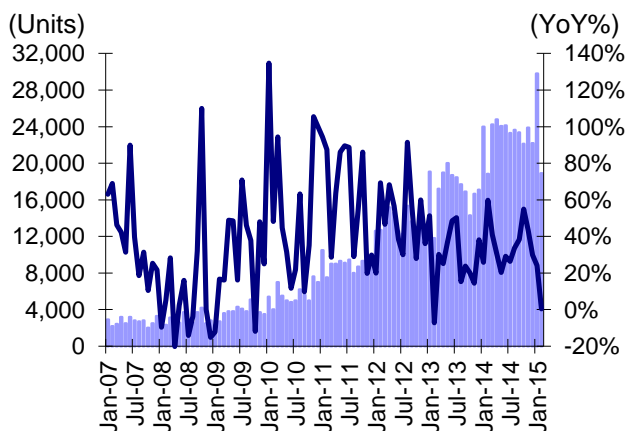
Brilliance now targets a growth rate of 10% for Brilliance BMW vehicle sales in FY15E, implying a volume target of about 306,382 units. In January-February, the JV recorded a sales volume growth rate of 13.7% YoY, to 48,701 units, above the company's full-year growth target. Despite cautious guidance, we are still optimistic that the Brilliance BMW JV can attain mid-teen sales volume growth in FY15-16E considering 1) still-solid demand in the existing model lineup, 2) upcoming local production of the 2-series Active Tourer in 2H15E, and 3) the replacement of the X1 SUV production with the new generation X1 in FY16E.

In addition, Sohu Auto News released some undercover photos in February showing that road testing of the all-new 1-series sedan has taken place in China. Since the 1-series sedan shares the same front-wheel-drive platform as the 2-series Active Tourer and the new generation X1, we have reason to believe the Brilliance BMW JV may localize the production of the 1-series sedan in China. Although the timing of the new launch, if true, is unknown, we believe it could happen in FY16-17E. Since this model is currently not in our forecast, given a lack of confirmation from BMW or Brilliance, including it would be an upside risk to our estimate. Also, the 1-series sedan can help further broaden BMW's customer base.

Another boost to Brilliance BMW sales, in our view, is the increasing adoption of automobile financing, which helps to further enlarge the potential customer base.

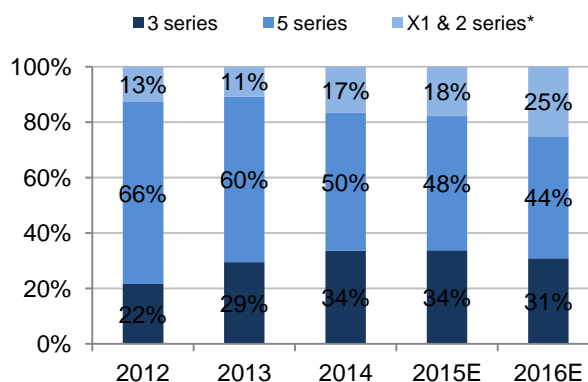
Regarding the product mix, we believe that while demand for the 5-series will still account for about 45-50% of total FY15E sales volume, contribution from the 3-series and X1 is likely to increase.

Figure 2: Brilliance BMW – monthly sales trend



Source: Company data

Figure 3: Brilliance BMW – product sales mix



*Remark: 2-series Active Tourer to be launched in 2H15E
 Source: Company data



We are prudent on FY15-16E margin, but not overly bearish

After years of positive operating leverage due to high utilization at BMW JV, we expect the margin expansion pace to halt, mainly because the product mix will skew further downward in terms of price range.

Nevertheless, we are optimistic that Brilliance BMW will manage to reap enough cost savings from further localization of engine production to offset the new spending; for example, more R&D expenses to localize new models. To elaborate, the JV has already achieved some cost savings by assembling engines in China with import components. By 2016E, Brilliance BMW's own engine production plant will also be completed and should bring the production cost down further by increasing the local component ratio.

Last but not least, there are likely to be additional margin drivers for the JV, as EUR depreciation would probably help the JV partially lower the unit cost of components imported from Europe.

Figure 4: Brilliance BMW – key financial data

	1H11	2H11	1H12	2H12	1H13	2H13	1H14	2H14
Sales volume (units)	55,012	53,177	80,792	80,057	105,692	101,037	140,013	138,516
YoY%	68.8%	40.3%	46.9%	50.5%	30.8%	26.2%	32.5%	37.1%
Revenue (RMBm)	17,772.2	19,759.6	26,107.5	30,043.1	37,244.9	35,927.6	48,243.4	46,301.8
YoY%	103.7%	54.9%	46.9%	52.0%	42.7%	19.6%	29.5%	28.9%
Pre-tax profit (RMBm)	1,732.1	1,702.7	3,537.8	3,535.6	5,661.7	3,560.0	9,886.6	4,891.2
YoY%	165.0%	16.4%	104.2%	107.6%	60.0%	0.7%	74.6%	37.4%
Operating profit margin (%)	9.7%	8.6%	13.6%	11.8%	15.2%	9.9%	20.5%	10.6%
Net profit (RMBm)	1,664.6	1,776.0	2,621.0	2,029.3	4,194.1	2,676.5	7,382.3	3,689.7
YoY%	190.1%	45.8%	57.5%	14.3%	60.0%	31.9%	76.0%	37.9%
Per vehicle profit (RMB)	30,258.0	33,397.4	32,441.9	25,348.5	39,682.1	26,490.4	52,725.7	26,637.4

Source: Company data, Deutsche Bank

Minibus/MPV business

Brilliance unveiled its Huasong 7-seat premium MPV at the Guangzhou Auto Show in November 2014. The product is developed with support from BMW and houses a BMW-technology-based engine. As a result of the new premium MPV model launch this week, despite the weak macroeconomic backdrop, Brilliance targets 28% minibus/MPV sales volume growth for FY15E. We believe that since it may take some time for the Huasong 7 sales to ramp up and initial margin could be low for the product, we prefer to maintain our conservative outlook on the minibus/MPV business for now, although it is unlikely to become a big earnings drag on Brilliance.



Upward earnings revision

Raising FY15-16E earnings on higher margin expectations

We do not have any significant changes to our revenue forecast for Brilliance. Meanwhile, we revise up our FY15-16 earnings contribution forecasts from the BMW JV by 5.1-5.9%, using higher margin assumptions, mainly driven by the more favorable RMB/EUR outlook. In summary, this leads to a 6.2-6.9% increase in our FY15-16 net profit forecasts.

Figure 5: Brilliance China – major assumptions underlying Deutsche Bank's forecast

	2012	2013	2014	2015E	2016E	2017E
Sales volume (units)						
Minibuses	82,506	83,747	77,710	84,994	92,170	99,236
YoY growth	0.0%	1.5%	-7.2%	9.4%	8.4%	7.7%
BMW sedans	160,849	206,729	278,529	316,693	382,089	434,112
YoY growth	48.7%	28.5%	34.7%	13.7%	20.6%	13.6%
Turnover (RMBm)*	5,916	6,103	5,515	6,307	6,860	7,390
YoY growth	-8.2%	3.2%	-9.6%	14.4%	8.8%	7.7%
Gross profit (RMBm)*	696	687	562	599	686	776
YoY growth	-18.6%	-1.4%	-18.1%	6.5%	14.5%	13.1%
Gross profit margin*	11.8%	11.2%	10.2%	9.5%	10.0%	10.5%
Contribution by BMW JV	2,325	3,435	5,536	6,123	6,936	7,927
YoY growth	35.2%	47.7%	61.2%	10.6%	13.3%	14.3%
Net profit	2,301	3,374	5,403	6,030	6,849	7,855
YoY growth	27.0%	46.6%	60.1%	11.6%	13.6%	14.7%

* Minibus and auto parts business only
Source: Company data, Deutsche Bank estimates



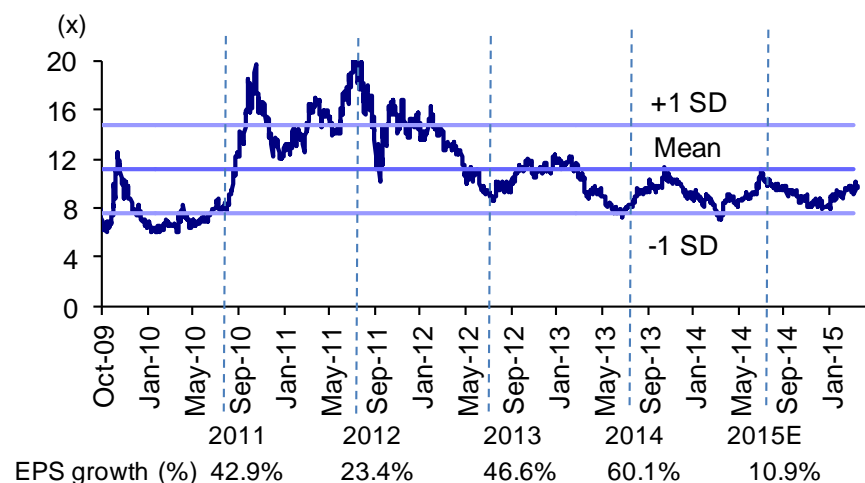
Valuation and risks

Premium valuation justified on earnings growth resilience

Our new target price of HKD17.2 is still based on 11.5x FY15E P/E, which is at a premium to the industry's long-term trading average of 11x, to reflect our optimism on the Brilliance BMW JV's long-term outlook. This is justified, in our view, by Brilliance's robust FY14-17E three-year earnings CAGR of 13%. The implied P/E-to-growth ratio stands at just 0.9x, which is by no means stretched, in our view.

With more than 20% upside potential, we maintain our Buy on Brilliance.

Figure 6: Brilliance China – rolling forward P/E band



Source: Company data, Bloomberg Finance LP, Deutsche Bank estimates

Risks

Key downside risks include an unexpected slowdown in luxury passenger vehicle demand, competition from other luxury brands' new models, and unexpected cost overruns.



Appendix 1

Important Disclosures

Additional information available upon request

Disclosure checklist

Company	Ticker	Recent price*	Disclosure
Brilliance China	1114.HK	14.30 (HKD) 26 Mar 15	7

*Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg and other vendors. Data is sourced from Deutsche Bank and subject companies.

Important Disclosures Required by U.S. Regulators

Disclosures marked with an asterisk may also be required by at least one jurisdiction in addition to the United States. See Important Disclosures Required by Non-US Regulators and Explanatory Notes.

7. Deutsche Bank and/or its affiliate(s) has received compensation from this company for the provision of investment banking or financial advisory services within the past year.

Important Disclosures Required by Non-U.S. Regulators

Please also refer to disclosures in the Important Disclosures Required by US Regulators and the Explanatory Notes.

7. Deutsche Bank and/or its affiliate(s) has received compensation from this company for the provision of investment banking or financial advisory services within the past year.

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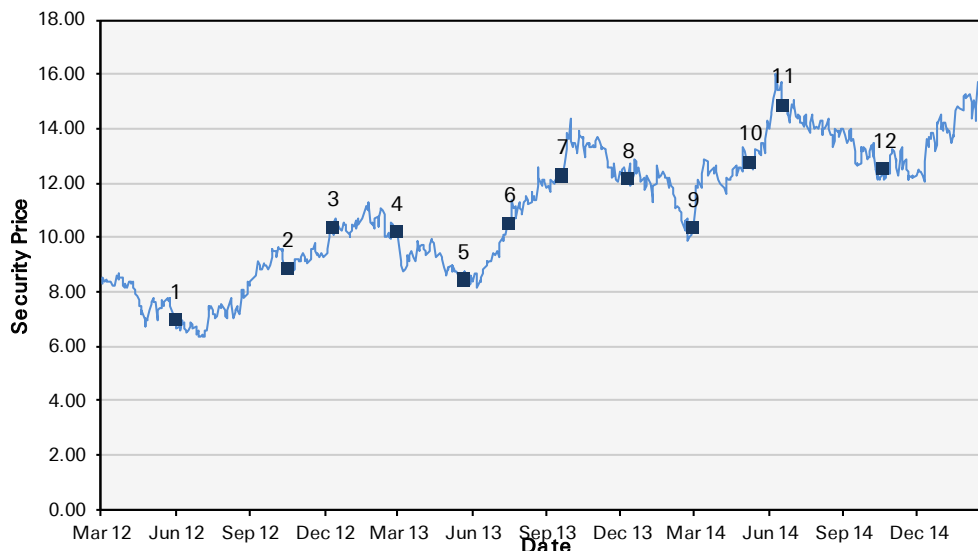
Analyst Certification

The views expressed in this report accurately reflect the personal views of the undersigned lead analyst(s) about the subject issuer and the securities of the issuer. In addition, the undersigned lead analyst(s) has not and will not receive any compensation for providing a specific recommendation or view in this report. Vincent Ha



Historical recommendations and target price: Brilliance China (1114.HK)

(as of 3/26/2015)



Previous Recommendations

- Strong Buy
- Buy
- Market Perform
- Underperform
- Not Rated
- Suspended Rating

Current Recommendations

- Buy
- Hold
- Sell
- Not Rated
- Suspended Rating

*New Recommendation Structure as of September 9, 2002

1.	28/06/2012:	Buy, Target Price Change HKD9.60	7.	17/10/2013:	Buy, Target Price Change HKD15.10
2.	13/11/2012:	Buy, Target Price Change HKD11.40	8.	06/01/2014:	Buy, Target Price Change HKD15.30
3.	08/01/2013:	Buy, Target Price Change HKD12.40	9.	27/03/2014:	Buy, Target Price Change HKD13.70
4.	27/03/2013:	Buy, Target Price Change HKD11.90	10.	05/06/2014:	Buy, Target Price Change HKD14.80
5.	17/06/2013:	Buy, Target Price Change HKD11.40	11.	15/07/2014:	Buy, Target Price Change HKD16.70
6.	13/08/2013:	Buy, Target Price Change HKD13.00	12.	17/11/2014:	Buy, Target Price Change HKD16.30

Equity rating key

Buy: Based on a current 12- month view of total share-holder return (TSR = percentage change in share price from current price to projected target price plus pro-jected dividend yield) , we recommend that investors buy the stock.

Sell: Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock

Hold: We take a neutral view on the stock 12-months out and, based on this time horizon, do not recommend either a Buy or Sell.

Notes:

1. Newly issued research recommendations and target prices always supersede previously published research.

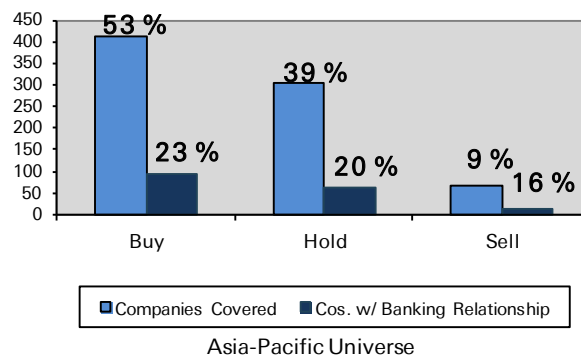
2. Ratings definitions prior to 27 January, 2007 were:

Buy: Expected total return (including dividends) of 10% or more over a 12-month period

Hold: Expected total return (including dividends) between -10% and 10% over a 12-month period

Sell: Expected total return (including dividends) of -10% or worse over a 12-month period

Equity rating dispersion and banking relationships





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