

Eyes on proprietary brand SUV

- BAIC reported a strong set of 1H16 results, with its proprietary brand the bright spot (60% YoY revenue growth on strong *Senova* SUV sales). Its GPM improved to 22% on higher SUV contribution from 40% to 59% in total volume during Jan-Jul.
- Revenue from Benz rose 28% on strong sales of *GLA* (+445% YoY) and *C-class* (+56% YoY), while a pickup in its *E-class* sales likely in 2H16.
- On the back of higher sales volume assumption in the new *E-class* and the proprietary SUVs, we revised up our FY16E/17E earnings by 8%/2%, and raised our price target to HKD8.3 (from HKD6.48), pegging on 2017E 10.0x PER. Maintain Buy rating.

Senova SUV drives proprietary brand sales. Due to the low profitability in its proprietary brand sedan segment, BAIC has continued to cut loss-making sedan business, with revenue contribution of *Senova* sedan dropping from 5.5% in Jan-16 to 1.4% in Jun-16 and sales volume sliding sharply from 42,281 units 1H15 to 6,659 units 1H16. As most *Senova* SUV models are manufactured on its sedan platform, BAIC's shift from sedan to SUV has not led to sharp costs increase, while higher SUV ASP helped boost gross margin in 1H16. With gross margin swung from loss to profit, BAIC reported RMB0.27mn in gross profit versus RMB0.71mn loss in 1H15. Looking forward, we expect to see further gross margin expansion in 2H16 and much narrower net loss at its proprietary brand segment for FY16E.

New E-class to drive JV Benz sales in 2H16. JV Benz sales jumped 39% from 103,034 in 1H15 to 143,398 in 1H16, driven by *GLA* (+445% YoY) and *C-class* (+56% YoY) despite 35% sales volume drop in its old *E-class*. During 1H16, some demand in its old *E-Class* has been delayed due to the launch of the much-expected new *E-class*, and hence likely a sales pickup of its old *E-class* in 2H16 in our view. Gross profit in JV Benz surged 52% YoY in 1H16 with gross margin expanding from 23.6% in 1H15 to 28.1% in 1H16. In spite of likely limited room for ASP growth in 2H16 (3.0T E-class to come later), strong sales volume growth would secure even stronger profit growth in JV Benz in 2H16 in our view.

Valuation. After raising our sales growth forecasts for proprietary brand (30% YoY) and JV Benz (22% YoY), we upped our FY16E/17E revenue by 5%/3% and earnings by 8%/2% respectively. We also raised our price target to HKD8.29 (from HKD6.48), pegging on 2017E 10.0x PER (prev. 2016E 10x). Maintain BUY rating.

BAIC (1958 HK)

Buy

(unchanged)

Price Target	HK\$8.3
(Revision)	(+28%)
(upside)	(7.5%)

EPS	2016E	2017E
revision	(8%)	(2%)

Close price	HKD7.72
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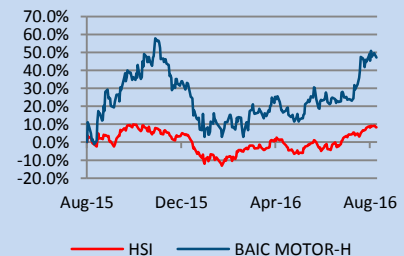
Market cap.	USD7,394mn
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Free float	39.7%
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3-mth ave. T/O	HKD15.5 mn
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Price as of 26 Aug 2016

Stock rel HSI performance (%)



Analysts

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Income statement (RMBm)

Year end: Dec	2014	2015	2016E	2017E	2018E
Revenue	56,370	84,112	104,613	122,878	137,651
COGS	(47,387)	(68,835)	(84,109)	(97,712)	(109,439)
Gross profit	8,983	15,277	20,504	25,165	28,212
Selling expenses	(5,647)	(8,002)	(10,011)	(11,595)	(12,932)
General and administrative	(3,455)	(4,039)	(4,740)	(5,090)	(5,472)
Other operating expenses					
EBITDA	2,245	7,022	9,877	12,925	14,599
Depreciation & Amortization	(2,364)	(3,787)	(4,125)	(4,445)	(4,790)
Other income	1,540	1,244	1,327	1,397	1,471
EBIT	1,422	4,479	7,080	9,878	11,280
Net interest	(533)	(416)	(532)	(446)	(487)
JVs and associates	5,809	4,257	4,258	3,963	3,868
Pretax profit	6,698	8,321	10,806	13,395	14,661
Taxation	(857)	(1,999)	(2,484)	(3,120)	(3,384)
Minority interests	(1,331)	(3,003)	(3,903)	(4,865)	(5,390)
Net profit	4,511	3,319	4,419	5,410	5,887
Net profit (adjusted)	4,511	3,319	4,419	5,410	5,887
Basic EPS (RMB)	0.70	0.44	0.58	0.71	0.78
Diluted EPS (RMB)	0.70	0.44	0.58	0.71	0.78
DPS (RMB)	0.30	0.15	0.23	0.28	0.31

Cash flow statement (RMBm)

Year end: Dec	2014	2015	2016E	2017E	2018E
EBIT	1,422	4,479	7,080	9,878	11,280
Depreciation & amortisation	2,364	3,787	4,125	4,445	4,790
Net interest	533	416	532	446	487
Taxes paid	(1,365)	(1,674)	(2,484)	(3,120)	(3,384)
Changes in working capital	1,282	4,649	908	299	(1,820)
Others	(1,974)	(1,291)	(1,063)	(893)	(975)
Cash flow from operations	2,262	10,365	9,096	11,055	10,378
Capex	(9,055)	(9,220)	(8,000)	(8,000)	(8,000)
Acquisitions	(6,229)	(4,372)	(3,979)	(4,174)	(4,379)
Disposals	807	4	-	-	-
Others	4,535	5,145	3,812	3,545	3,459
Cash flow from investing	(9,941)	(8,444)	(8,167)	(8,629)	(8,920)
Dividends	(2,793)	(2,780)	(1,189)	-	-
Issue of shares	7,910	613	-	-	-
Change in debt	7,396	343	3,392	1,163	3,805
Others	300	1,925	-	-	-
Cash flow from financing	12,813	102	2,253	1,163	3,805
Change in cash	5,133	2,023	3,182	3,589	5,263
Free cash flow	(6,793)	1,145	1,096	3,055	2,378

Balance sheet (RMBm)

Year end: Dec	2014	2015	2016E	2017E	2018E
Cash	21,923	23,946	27,129	30,717	35,981
Short term investments	-	-	-	-	-
Accounts receivables	6,422	10,949	17,518	28,028	44,845
Inventory	11,068	9,871	11,894	14,321	17,234
Other current assets	4,905	7,471	7,758	8,133	8,608
Total current assets	44,319	52,237	64,297	81,200	106,668
PP&E	34,218	38,353	42,889	47,149	51,109
Intangible Assets	8,251	11,473	14,916	18,511	22,265
Associates and JVs	14,066	14,582	15,029	15,447	15,857
Other long term assets	9,004	10,748	12,000	12,975	14,159
Total long term assets	65,540	75,156	84,835	94,083	103,389
TOTAL ASSETS	109,859	127,393	149,132	175,283	210,057
Short term debt	15,983	21,280	23,607	24,409	27,747
Accounts payables	14,978	21,382	29,935	41,909	58,673
Other current liabilities	20,539	24,965	26,976	29,076	31,341
Total current liabilities	51,500	67,627	80,518	95,395	117,761
Long term debt	13,935	8,986	10,051	10,412	10,879
Deferred tax	887	840	865	891	918
Convertible bonds					
Other long term liabilities	1,568	2,871	3,445	4,058	4,696
Total long term liabilities	16,390	12,697	14,361	15,361	16,493
TOTAL LIABILITIES	67,890	80,324	94,880	110,756	134,254
Shareholders' funds	33,355	35,010	38,290	43,700	49,587
Minority interests	8,614	12,059	15,962	20,827	26,217
TOTAL LIAB AND EQUITY	109,859	127,393	149,132	175,283	210,057
Net cash / (debt)	(7,995)	(6,320)	(6,529)	(4,103)	(2,645)

Source: CSC Research estimates

Key ratios

Year end: Dec	2014	2015	2016E	2017E	2018E
Operating ratios					
Gross margin	15.9	18.2	19.6	20.5	20.5
EBITDA margin (%)	4.0	8.3	9.4	10.5	10.6
Effective tax rate (%)	12.8	24.0	23.0	23.3	23.1
Revenue growth (%)	34.10	49.2	24.4	17.5	12.0
Net income growth (%)	66.2	(26.4)	33.2	22.4	8.8
EPS growth adj (%)	45.3	(37.8)	33.2	22.4	8.8
DPS growth (%)	(6.7)	(50.5)	55.0	22.4	8.8
Efficiency ratios					
ROE (%)	13.5	9.5	11.5	12.4	11.9
ROCE (%)	2.2	6.0	8.3	10.5	10.9
Asset turnover (x)	0.5	0.7	0.7	0.7	0.7
Op cash / EBIT (x)	1.6	2.3	1.3	1.1	0.9
Depreciation / CAPEX (x)	0.3	0.4	0.5	0.6	0.6
Accounts receivable days	40.2	37.7	49.7	67.6	96.6
Accounts payable days	100.5	96.4	111.3	134.2	167.7
Leverage ratios					
Net gearing (%)	24.0	18.1	17.1	9.4	5.3
Net debt / EBITDA (x)	3.6	0.9	0.7	0.3	0.2
Interest cover (x)	2.7	10.8	13.3	22.1	23.1
Current ratio (x)	0.9	0.8	0.8	0.9	0.9
Valuation					
PER (x)	9.2	14.8	11.1	9.1	8.3
EV/EBITDA (x)	29.0	9.6	7.2	5.7	5.3
PBR (x)	1.5	1.4	1.3	1.1	1.0
Dividend yield (x)	4.7	2.3	3.6	4.4	4.8



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Company Rating Definition

The Benchmark: Hong Kong Hang Seng Index; Time Horizon: 12 months

Buy	12-month absolute total return: $\geq 10\%$
Hold	12-month absolute total return: $> -10\%$ but $< 10\%$
Sell	12-month absolute total return: $\leq -10\%$

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