

Bitauto Holdings (BITA US)

Buy: Transforming into integrated online auto platform

- Used cars and auto financing to drive future growth
- 3Q results broadly in line; margin should bottom in 4Q
- Maintain Buy, target price unchanged at USD35

Used-cars and auto financing to drive future growth: Bitauto plans to focus on auto financing, as well as the used car market, to drive future growth. Since 2006, Bitauto has been exploring potential business opportunities in the used car market. Currently, the company generates sizable revenue in this market from 1) listing and advertising, transaction services (20-30% of revenue), and 2) auto financing products (70% of revenue). At its 3Q results, the company guided for the used car segment to contribute RMB400-500m revenue in FY16, and RMB1-1.5bn in FY17. Management expects to complete c100,000 revenue-generating used car transactions this year, and expects the number of transactions to at least double in 2017, accounting for 40% of total transactions by then. Per unit revenue is currently cRMB4,500, which management expects to improve to the RMB7,000 level long term. The company will disclose used car revenue as a separate segment versus new car revenue starting from 4Q16. We also expect the used car market to fuel the auto financing arm's growth. On auto financing, the company guides for the total loan size of its auto financing arm at RMB12-14bn in 2016, continuing to grow rapidly in 2017.

Margin to bottom in 4Q: Since July 2016, Bitauto has been scaling down its loss-making businesses YiChe Mall and Auto Agent. The impact could lead to short-term margin pressure due to 1) one-off administration costs and 2) selling existing inventories. We expect a Q4 non-GAAP operating margin of 8.7%, down 2 ppts sequentially. But in the long run, Bitauto's headcount expansion should slow down significantly and support margin expansion. The scaling down of loss-making business will also allow Bitauto to reallocate resources to more promising business.

3Q16 results and 4Q16e guidance broadly in line: Bitauto's 3Q16 revenue was RMB1.5bn, c5-6% higher than HSBC and consensus estimates. Net income was 4% lower than our expectation mainly due to 1) high interest expense related to the expanding auto financing business and 2) sizeable shared losses from associates and joint ventures. Management guides for 4Q16 revenue to be in the range of RMB1,580-1,630m, in line with consensus. Historically the company has beaten mid-range guidance by 1-9%.

Maintain Buy rating and target price of USD35: We cut our 2016-18e net profit by 3-13% on lower margin assumptions and higher non-operating expenses. The effect is partly offset by a lower risk-free rate assumption and WACC, meaning our DCF-based target price is unchanged after rounding. We maintain our Buy rating on Bitauto as we expect margins to bottom in coming quarter, and the used car market and auto financing to drive robust future growth. **Key downside risk:** slower auto industry growth.

EQUITIES INTERNET

China



MAINTAIN BUY

TARGET PRICE (USD)

35.00

PREVIOUS TARGET (USD)

35.00

SHARE PRICE (USD)

25.25

(as of 09 Nov 2016)

UPSIDE/DOWNSIDE

+38.6%

MARKET DATA

Market cap (USDm)	1,786	Free float	100%
Market cap (USDm)	1,786	BBG	BITA US
3m ADTV (USDm)	29	RIC	BITA.N

FINANCIALS AND RATIOS (CNY)

Year to	12/2015a*	12/2016e	12/2017e	12/2018e
HSBC EPS	3.64	5.66	9.75	14.23
HSBC EPS (prev)	4.70	6.50	10.51	14.60
Change (%)	-22.6	-12.9	-7.2	-2.5
Consensus EPS	5.14	6.04	10.73	15.59
PE (x)	47.1	30.3	17.6	12.0
Dividend yield (%)	0.0	0.0	0.0	0.0
EV/EBITDA (x)	-	10.9	5.8	2.9
ROE (%)	4.0	4.9	8.1	11.4

*2015a restated for changed US GAAP accounting

52-WEEK PRICE (USD)



Source: Thomson Reuters IBES, HSBC estimates

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This report must be read with the disclosures and the analyst certifications in the Disclosure appendix, and with the Disclaimer, which forms part of it.

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Financials & valuation: Bitauto Holdings

Buy

Financial statements

Year to	12/2015a	12/2016e	12/2017e	12/2018e
Profit & loss summary (CNYm)				
Revenue	4,012	5,653	7,009	8,742
EBITDA	-66	551	878	1,281
Depreciation & amortisation	-570	-674	-738	-770
Operating profit/EBIT	-636	-124	140	511
Net interest	17	-17	-6	-5
PBT	-508	-166	114	492
HSBC PBT	-388	-81	275	682
Taxation	-65	-101	-133	-194
Net profit	-572	-267	-19	298
HSBC net profit	212	438	754	1,100

Cash flow summary (CNYm)

Cash flow from operations	-2,504	619	1,116	1,585
Capex	-232	-189	-189	-189
Cash flow from investment	-3,508	-189	-189	-189
Dividends	0	0	0	0
Change in net debt	-1,758	-2,330	-892	-1,351
FCF equity	-2,959	275	722	1,090

Balance sheet summary (CNYm)

Intangible fixed assets	2,913	2,300	1,688	1,075
Tangible fixed assets	849	1,067	1,243	1,426
Current assets	7,534	10,399	11,601	13,323
Cash & others	3,041	5,371	6,263	7,614
Total assets	12,069	14,539	15,304	16,597
Operating liabilities	2,347	3,050	3,673	4,478
Gross debt	0	0	0	0
Net debt	-3,041	-5,371	-6,263	-7,614
Shareholders' funds	8,492	9,285	9,426	9,914
Invested capital	5,908	5,345	4,595	3,732

Ratio, growth and per share analysis

Year to	12/2015a	12/2016e	12/2017e	12/2018e
Y-o-y % change				
Revenue	63.1	40.9	24.0	24.7
EBITDA	-111.0		59.5	45.9
Operating profit	-218.2			264.8
PBT	-186.5			330.0
HSBC EPS	-68.2	55.4	72.2	45.9

Ratios (%)

Revenue/IC (x)	1.2	1.0	1.4	2.1
ROIC	-4.1	14.0	-2.5	16.3
ROE	4.0	4.9	8.1	11.4
ROA	-7.2	-1.4	-0.2	2.1
EBITDA margin	-1.6	9.7	12.5	14.7
Operating profit margin	-15.9	-2.2	2.0	5.9
EBITDA/net interest (x)	3.9	32.2	151.7	281.9
Net debt/equity	-35.3	-57.1	-65.6	-75.9
Net debt/EBITDA (x)	46.3	-9.8	-7.1	-5.9
CF from operations/net debt				

Per share data (CNY)

EPS Rep (diluted)	-9.84	-3.45	-0.24	3.85
HSBC EPS (diluted)	3.64	5.66	9.75	14.23
DPS	0.00	0.00	0.00	0.00
Book value	146.05	136.32	138.40	145.55

Valuation data

Year to	12/2015a	12/2016e	12/2017e	12/2018e
EV/sales	2.1	1.1	0.7	0.4
EV/EBITDA	-	10.9	5.8	2.9
EV/IC	1.4	1.1	1.1	1.0
PE*	47.1	30.3	17.6	12.0
PB	1.2	1.3	1.2	1.2
FCF yield (%)	-26.1	2.4	6.4	9.6
Dividend yield (%)	0.0	0.0	0.0	0.0

* Based on HSBC EPS (diluted)

Issuer information

Share price (USD)	25.25	Free float	100%
Target price (USD)	35.00	Sector	Internet
Reuters (Equity)	BITA.N	Country	China
Bloomberg (Equity)	BITA US	Analyst	Terry Chen, CFA
Market cap (USDm)	1,786	Contact	+852 2996 6635

Price relative



Source: HSBC

Note: Priced at close of 09 Nov 2016

Third quarter results and earnings revisions

3Q16 results

(RMBm)	3Q16 results			Delta		4Q16e		
	Actual	HSBCe	Consensus	vs. HSBCe	vs. Cons.	Guidance	HSBC	Consensus
Revenue	1,500	1,425	1,417	5%	6%	1,605	1,813	1,612
Advertising and subscription	898	939		-4%				
Transaction service	404	360		12%				
Digital marketing solutions	198	127		56%				
Gross profit	958	870		10%				
Non-GAAP operating profit	159	146		9%				
Non-GAAP net income	129	135	146	-4%	-11%			
Non-GAAP EPS (USD)	0.16	0.33	0.27	-51%	-40%			

Source: Company data, Bloomberg consensus, HSBC estimates

Quarterly profit & loss statement

(RMB'000)	Restated 1Q15	Restated 2Q15	Restated 3Q15	Restated 1Q16	Restated 2Q16	Restated 3Q16	4Q16e
Revenues	740,457	1,061,299	1,126,888	1,083,504	1,391,413	1,499,889	1,678,274
Advertising & subscription	607,115	771,100	818,200	714,500	890,300	898,300	955,218
Transaction service	29,136	183,800	225,700	201,400	308,300	403,700	521,600
Digital marketing solutions	104,175	106,400	82,900	167,604	192,800	197,900	201,461
Cost of revenues	(241,607)	(379,228)	(407,125)	(352,503)	(540,936)	(541,402)	(628,532)
Gross profit	498,851	682,071	719,764	731,000	850,477	958,487	1,049,741
Gross margin (%)	67.4%	64.3%	63.9%	67.5%	61.1%	63.9%	62.5%
Operating expenses	(512,689)	(730,494)	(772,928)	(808,640)	(850,851)	(972,464)	(1,081,491)
Income/(loss) from operations	(13,838)	(48,423)	(53,164)	(77,640)	(373)	(13,977)	(31,750)
Non-GAAP operating profit	34,122	128,281	139,190	99,477	169,394	158,835	145,839
Non-GAAP operating profit margin	4.6%	12.1%	12.4%	9.2%	12.2%	10.6%	8.7%
GAAP Net income	60,453	(55,179)	(77,721)	(108,209)	(47,504)	(48,057)	(63,040)
Non-GAAP net income	18,599	122,567	114,887	69,196	124,763	129,260	114,550
Non-GAAP net margin	2.5%	11.5%	10.2%	6.4%	9.0%	8.6%	6.8%
EPS - Basic (USD)	0.05	0.31	0.28	0.07	0.21	0.16	0.14

Source: Company data, HSBC estimates

Quarterly actual results earning versus guidance

(RMBm)	4Q15	1Q16	2Q16	3Q16	4Q16e	QoQ (%)	YoY (%)
Revenue guidance	1,200-1,230	1,050-1,090	1,350-1,400	1,370-1,420	1,580-1,605		
Low-end	1,200	1,050	1,350	1,370	1,580	5.3%	19.2%
High-end	1,230	1,090	1,400	1,420	1,630	8.7%	23.0%
Mid-point	1,215	1,070	1,375	1,395	1,605	7.0%	21.1%
Actual	1,326	1,084	1,391	1,425			
Beat/(miss)	9.1%	1.3%	1.2%	2.2%			

Source: Company data

Annual profit & loss

(RMB'000)	2016e	2017e	2018e
Revenues	5,653,079	7,009,433	8,742,407
Advertising and subscription	3,458,318	3,832,092	4,237,147
Transaction service	1,435,000	2,037,700	2,852,780
Digital marketing solutions	759,761	1,139,641	1,652,480
Cost of revenues	(2,063,374)	(2,628,537)	(3,278,403)
Gross profit	3,589,705	4,380,896	5,464,004
Gross margin (%)	63.5%	62.5%	62.5%
Operating expenses	(3,713,447)	(4,240,707)	(4,952,573)
Income/(loss) from operations	(123,741)	140,189	511,431
Non-GAAP operating income/(loss)	573,545	892,868	1,298,769
Non-GAAP operating margin (%)	10.1%	12.7%	14.9%
GAAP Net income	(266,810)	1,340	312,753
Non-GAAP net income	437,769	754,019	1,100,092
YoY growth (%)	106.7%	72.2%	45.9%
Non-GAAP net margin (%)	7.7%	10.8%	12.6%
EPS (USD)	0.9	1.6	2.4

Source: HSBC estimates

Estimate changes

(RMBm)	2016e	2017e	2018e
Current			
Total revenue	5,653	7,009	8,742
Non-GAAP operating margin	10.1%	12.7%	14.9%
Non-GAAP net margin	7.7%	10.8%	12.6%
EPS (USD)	0.95	1.63	2.38
Previous			
Total revenue	5,713	7,028	8,727
Non-GAAP operating margin	10.5%	13.1%	14.7%
Non-GAAP net margin	8.8%	11.6%	12.9%
EPS (USD)	1.1	1.8	2.4
Delta			
Total revenue	-1%	0%	0%
Non-GAAP operating margin	0	0	0
Non-GAAP net margin	-1	-1	0
EPS (USD)	-13%	-7%	-3%

Source: HSBC estimates

Earnings estimate revisions: We cut our 2016 revenue forecast by c1% on slower-than-expected traditional business (advertising and subscription segment) growth. Our 2017-18 revenue estimates are barely changed. We trim our 2016-17e operating margins by 0.3-0.4 ppt to reflect the one-off cost from the discontinuation of the YiChe Mall and Auto Agent businesses. We expect higher interest expense in 2016-18, mainly due to the expansion of the auto financing business. As a result, we have cut our net profit margin forecasts by c1 ppts in 2016-17. Our 2018 margin assumptions are little changed. We have reduced our EPS estimates by 3-13% in 2016-18e, mainly due to our higher non-operating expense assumptions.

Valuation and risks

We maintain our Buy rating on the stock and our target price of USD35. Our investment thesis rests on two points. First, the transaction service business will likely become a new growth engine for Bitauto with improved profitability. Second, as an integrated online automotive platform, Bitauto has the opportunity to tap into auto financing and after-sales services, which provides an option value for the stock.

We derive our target price using a 10-year DCF model. Our key assumptions are a lower WACC of 18.1% and a 2% terminal growth rate. Our WACC of 18.1% (was 18.6%) is calculated using a 2.5% risk-free rate (was 3.0%), a 2.6 equity beta from Bloomberg, a 6% equity risk premium and the assumption that Bitauto will remain debt-free in the long term. We adjust our risk-free rate to reflect the latest HSBC cost of equity assumptions; our other assumptions are unchanged. The effect of our lower earnings estimate is offset by the lower WACC. Our rounded USD35 target price is unchanged and implies 39% upside.

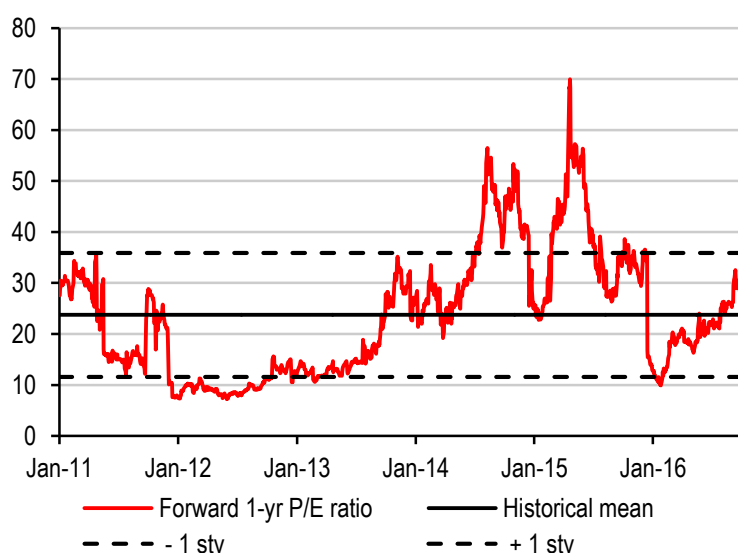
Currently, Bitauto is trading at 30x and 18x 2016/17e PE on our estimates compared with 35x and 21x for China Internet peers. Bitauto is currently trading at 28x Bloomberg forward PE, largely in line with the historical average of 24x.

DCF valuation for Bitauto

	2016e	2017e	2018e	2024e	2025e	2026e
Revenue (RMBm)	5,653	7,009	8,742	12,906	15,361	17,872
EBITDA (RMBm)	551	878	1,281	1,924	2,279	3,006
EBITDA margin (%)	9.7%	12.5%	14.7%	20.6%	22.3%	24.0%
FCF (RMBm)	270	674	1,042	1,622	1,695	2,282
WACC (%)	18.1%					
Terminal growth rate (%)	2.0%					
Implied terminal EV/EBITDA (x)	4.9					
Enterprise value (RMBbn)	14,770					
Net cash (RMBbn)	3,895					
Equity value (RMBbn)	18,664					
Equity value (RMB per share)	241					
Equity value (USD per share)	35					

Source: HSBC estimates

Bitauto historical forward PE



Source: Bloomberg

China Internet comp table

Company	Ticker	Rating	Currency	Market cap (USDbn)	Share price 9-Nov-16	Target price	Upside/downside	PE 2016e	PE 2017e
Alibaba	BABA US	Buy	USD	247	96.67	120	24%	28.2	21.3
Tencent	700 HK	Buy	HKD	247	202.40	256	26%	35.6	23.2
Baidu	BIDU US	Buy	USD	59	168.66	216	28%	34.0	20.9
JD.com	JD US	Buy	USD	37	25.13	32	27%	nm	nm
Ctrip	CTRP US	Hold	USD	26	42.29	46	9%	115.5	31.9
Vipshop	VIPS US	Buy	USD	7	12.92	23	78%	19.0	13.6
58.com	WUBA US	Buy	USD	6	40.20	66	64%	nm	45.4
SINA	SINA US	Buy	USD	5	71.78	91.19	27%	46.8	21.2
Momo	MOMO US	Buy	USD	3	23.51	35	49%	34.4	20.2
YY	YY US	Buy	USD	3	46.91	61	30%	12.9	10.5
Autohome	ATHM US	Buy	USD	3	23.86	35	47%	15.5	13.8
Sohu	SOHU US	Buy	USD	1	35.39	59	67%	n.a	n.a
Changyou	CYOU US	Buy	USD	1	26.81	30	12%	9.9	8.6
Average								35.2	21.0

Source: Bloomberg, HSBC estimates

Key downside risks

Macro

Bitauto's operational results are highly correlated to the automotive industry. Our base case is that the auto industry could sustain the growth rate in sales volume of 5-10% in the coming years. If the growth rate turns out to be significantly lower than this range or even negative, automakers and dealers could cut their advertising budgets or shift budgets from advertising to direct sales rebates to consumers. As a result, Bitauto's revenue growth could be significantly lower than our forecasts. As a pure online auto advertising platform, we think it is unlikely Bitauto would escape the drag from the real economy.

Investments in mobile and new business initiatives

Our base case is that Bitauto will control spending, especially on sales and marketing expenses, to adjust to slower revenue growth. The company will continue to spend on mobile, e-commerce, and used auto businesses, but we expect expenses to grow more slowly than revenue, and the margin to gradually improve in future years. If Bitauto puts market share ahead of profitability or makes strategic investments in new businesses at the expense of margin, its profitability could be much lower than our forecasts.

Disclosure appendix

Analyst Certification

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Important disclosures

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From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 10 November 2016, the distribution of all independent ratings published by HSBC is as follows:

Buy	44%	(25% of these provided with Investment Banking Services)
Hold	40%	(26% of these provided with Investment Banking Services)
Sell	16%	(20% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

For the distribution of non-independent ratings published by HSBC, please see the disclosure page available at <http://www.hsbcnet.com/gbm/financial-regulation/investment-recommendations-disclosures>.

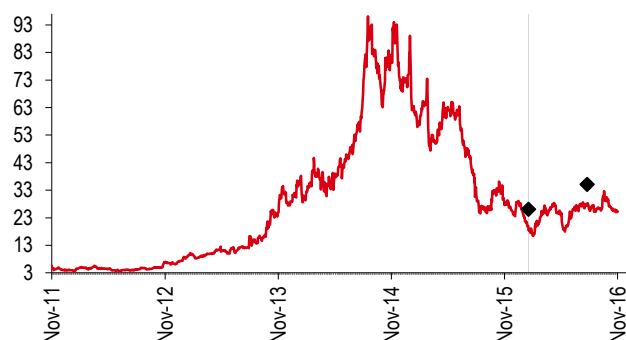
Share price and rating changes for long-term investment opportunities

Bitauto Holdings (BITA.N) share price performance USD
Vs HSBC rating history

Rating & target price history

From	To	Date	Analyst
N/A	Buy	27 Jan 2016	Terry Chen
Target price	Value	Date	Analyst
Price 1	26.00	27 Jan 2016	Terry Chen
Price 2	35.00	03 Aug 2016	Terry Chen

Source: HSBC



Source: HSBC

To view a list of all the independent fundamental ratings disseminated by HSBC during the preceding 12-month period, please see the disclosure page available at www.research.hsbc.com/A/Disclosures.

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price date	Disclosure
BITAUTO HOLDINGS	BITA.N	25.25	09-Nov-2016	6, 7

Source: HSBC

- 1 HSBC has managed or co-managed a public offering of securities for this company within the past 12 months.
- 2 HSBC expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.
- 3 At the time of publication of this report, HSBC Securities (USA) Inc. is a Market Maker in securities issued by this company.
- 4 As of 31 October 2016 HSBC beneficially owned 1% or more of a class of common equity securities of this company.
- 5 As of 30 September 2016, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of investment banking services.
- 6 As of 30 September 2016, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of non-investment banking securities-related services.
- 7 As of 30 September 2016, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of non-securities services.

- 8 A covering analyst/s has received compensation from this company in the past 12 months.
- 9 A covering analyst/s or a member of his/her household has a financial interest in the securities of this company, as detailed below.
- 10 A covering analyst/s or a member of his/her household is an officer, director or supervisory board member of this company, as detailed below.
- 11 At the time of publication of this report, HSBC is a non-US Market Maker in securities issued by this company and/or in securities in respect of this company
- 12 As of 04 November 2016, HSBC beneficially held a net long position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology.
- 13 As of 04 November 2016, HSBC beneficially held a net short position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology.

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