

Bitauto Holdings (BITA US)

Buy: Unlocking value

**EQUITIES
INTERNET**

China

- Equity fundraising and potential IPO to unlock value of Yixin
- Platform services will support long-term growth
- Maintain Buy and new TP of USD33 (was USD27)

Injecting all used auto business into Yixin. Yixin Capital, the e-financing and transaction service arm of Bitauto, announced it is entering into agreements with strategic investors including Tencent, China Orient AMC International, and the founder of SF Express on a new round of fundraising, which values the entity at USD3.5-4bn. Besides auto financing, Bitauto will inject all its used auto business including advertising and sales facilitation into Yixin Capital. Bitauto will still own not less than 48% of Yixin Capital post the fundraising.

Platform strategy. The auto financing revenue growth is currently funded by Yixin Capital's own balance sheet. It is thus not surprising to see Yixin Capital continuing to use equity financing to support growth. As it is operated independently, it could be separately listed in the future. Longer term, management expects Yixin Capital to outsource its risk assessment and servicing capability to third-party financing companies, and charge commission based on the transactions facilitated. As of 1Q'17, platform services account for 10% of the transaction revenue and 25% of net profit and for FY 2017, Bitauto expects it to contribute 33% and 50%, respectively. If Bitauto is successful in its platform strategy, growth in its transaction business should be more sustainable in the long term as it will become less reliant on balance sheet expansion.

Stable traditional business. After injecting the used auto business into Yixin Capital, Bitauto will mainly operate its traditional businesses including new car advertising and subscription and digital marketing solutions. For 2017, the company expects the traditional businesses to generate profit of RMB350m: in 1Q'17, these grew 4% y-o-y only, due to weak auto industry growth. We think growth momentum will remain sluggish unless the company significantly augments its content offering.

Maintain Buy rating, raise TP to USD33 (from USD27). We increase our 2017-19 earning estimates by 15-17% to factor in higher-than-expected growth in platform transaction services. We change our valuation methodology from DCF to sum-of-the-part in order to better reflect the valuation of Yixin Capital. We value Bitauto's 48% stake in Yixin Capital at USD1.7bn, consistent with the latest round of fundraising. We value Bitauto's traditional business at USD486m, which implies 10x 2017e PE. Our new TP implies upside of 6.1% and we rate the stock Buy, as we believe the fast progress in platform strategy in Yixin Capital may further improve the company fundamentals in the future. An IPO of Yixin Capital could be a potential future catalyst in our view. Key downside risks include slower-than-expected growth in auto sales volume.



MAINTAIN BUY

TARGET PRICE (USD)

33.00

PREVIOUS TARGET (USD)

27.00

SHARE PRICE (USD)

31.10

(as of 12 May 2017)

UPSIDE/DOWNSIDE

+6.1%

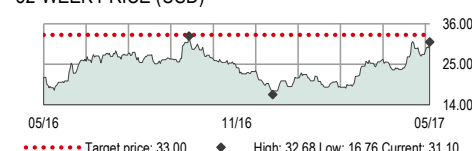
MARKET DATA

Market cap (USDm)	2,200	Free float	100%
Market cap (USDm)	2,200	BBG	BITA US
3m ADTV (USDm)	43	RIC	BITA.N

FINANCIALS AND RATIOS (CNY)

Year to	12/2016a	12/2017e	12/2018e	12/2019e
HSBC EPS	6.35	9.37	11.25	13.61
HSBC EPS (prev)	-	8.03	9.71	11.84
Change (%)	-	16.7	15.9	14.9
Consensus EPS	4.01	8.24	11.02	13.98
PE (x)	33.8	22.9	19.1	15.8
Dividend yield (%)	0.0	0.0	0.0	0.0
EV/EBITDA (x)	15.0	11.4	8.3	5.8
ROE (%)	4.9	7.0	8.3	9.8

52-WEEK PRICE (USD)



Source: Thomson Reuters IBES, HSBC estimates

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Financials & valuation: Bitauto Holdings

Buy

Financial statements

Year to	12/2016a	12/2017e	12/2018e	12/2019e
Profit & loss summary (CNYm)				
Revenue	5,773	7,249	8,776	10,478
EBITDA	597	735	884	1,059
Depreciation & amortisation	-686	-750	-781	-797
Operating profit/EBIT	-89	-14	103	262
Net interest	-11	8	13	12
PBT	-144	-27	101	264
HSBC PBT	-67	138	292	484
Taxation	-148	-114	-137	-166
Net profit	-291	-141	-36	98
HSBC net profit	439	648	779	942

Cash flow summary (CNYm)

Cash flow from operations	690	833	1,234	1,489
Capex	-189	-189	-189	-189
Cash flow from investment	-189	-189	-189	-189
Dividends	0	0	0	0
Change in net debt	-2,399	-609	-1,005	-1,245
FCF equity	288	534	798	995

Balance sheet summary (CNYm)

Intangible fixed assets	2,288	1,664	1,040	416
Tangible fixed assets	1,087	1,343	1,551	1,765
Current assets	10,388	11,364	12,655	14,165
Cash & others	5,440	6,049	7,055	8,300
Total assets	14,535	15,144	16,018	17,119
Operating liabilities	3,069	3,653	4,373	5,156
Gross debt	0	0	0	0
Net debt	-5,440	-6,049	-7,055	-8,300
Shareholders' funds	9,262	9,286	9,441	9,759
Invested capital	5,254	4,669	3,818	2,891

Ratio, growth and per share analysis

Year to	12/2016a	12/2017e	12/2018e	12/2019e
Y-o-y % change				
Revenue	35.7	25.6	21.1	19.4
EBITDA	452.1	23.2	20.3	19.8
Operating profit				154.3
PBT				160.7
HSBC EPS	0.5	47.6	20.1	21.0

Ratios (%)

Revenue/IC (x)	1.0	1.5	2.1	3.1
ROIC	19.4	65.2	-6.1	9.8
ROE	4.9	7.0	8.3	9.8
ROA	-1.4	1.0	-0.4	0.7
EBITDA margin	10.3	10.1	10.1	10.1
Operating profit margin	-1.5	-0.2	1.2	2.5
EBITDA/net interest (x)	56.8			
Net debt/equity	-58.0	-64.3	-73.8	-84.0
Net debt/EBITDA (x)	-9.1	-8.2	-8.0	-7.8
CF from operations/net debt				

Per share data (CNY)

EPS Rep (diluted)	-4.21	-2.04	-0.52	1.42
HSBC EPS (diluted)	6.35	9.37	11.25	13.61
DPS	0.00	0.00	0.00	0.00
Book value	142.15	142.51	144.89	149.76

Valuation data

Year to	12/2016a	12/2017e	12/2018e	12/2019e
EV/sales	1.6	1.2	0.8	0.6
EV/EBITDA	15.0	11.4	8.3	5.8
EV/IC	1.7	1.8	1.9	2.1
PE*	33.8	22.9	19.1	15.8
PB	1.5	1.5	1.5	1.4
FCF yield (%)	2.0	3.7	5.5	6.9
Dividend yield (%)	0.0	0.0	0.0	0.0

* Based on HSBC EPS (diluted)

Issuer information

Share price (USD)	31.10	Free float	100%
Target price (USD)	33.00	Sector	Internet
Reuters (Equity)	BITA.N	Country	China
Bloomberg (Equity)	BITA US	Analyst	Terry Chen, CFA
Market cap (USDm)	2,200	Contact	+852 2996 6635

Price relative



Source: HSBC

Note: Priced at close of 12 May 2017

Bitauto reported in-line 1Q'17 revenue while non-GAAP EPS beat consensus by 21%, mainly due to slower-than-expected headcount expansion and temporarily low spending in this quarter. The traditional business grew only 4% y-o-y while transaction services (mainly from Yixin Capital) grew 193.5% y-o-y. The company guides 2Q17e revenue to be in the range of RMB1,830-1,880m, which implies c32% y-o-y growth.

1Q'17 results

(Rmb mn)	1Q17 results			Delta		2Q17e	
	Actual	Consensus	Guidance	vs Cons.	vs Guidance	Guidance	Consensus
Revenue	1,545	1,535	1,505	1%	3%	1855	1,829
Advertising and subscription	745						
Transaction service	626						
Digital marketing solutions	175						
Gross profit	1,026						
Non-GAAP operating profit	223						
Non-GAAP net income	157	111		41%			
Non-GAAP EPS (USD)	0.18	0.15		21%			

Source: Company reports, Bloomberg, HSBC

We raise our EPS forecasts for 2017-19e by 17%/16%/15%, primarily due to 1) a c2-3% increase in our revenue estimates on faster-than-expected platform services revenue growth attributable to Yixin Capital, and 2) c1ppt increase in Non GAAP operating margin estimate, mainly on slower-than-expected headcount expansion. We also expect faster growth in the platform services business to support margin, as this business generates a relatively high margin.

Earnings revision table

(Rmb mn)	2017e	2018e	2019e
Current			
Total revenue	7,249	8,776	10,478
Non-GAAP operating margin	10.4%	10.3%	10.5%
Non-GAAP net margin	8.9%	8.9%	9.0%
EPS (USD)	1.38	1.66	2.01
Previous			
Total revenue	7,005	8,544	10,309
Non-GAAP operating margin	9.4%	9.3%	9.4%
Non-GAAP net margin	7.9%	7.9%	7.9%
EPS (USD)	1.2	1.4	1.7
Delta			
Total revenue	3%	3%	2%
Non-GAAP operating margin (ppt)	1.0	1.0	1.1
Non-GAAP net margin (ppt)	1.0	1.0	1.1
EPS (USD)	17%	16%	15%

Source: Company reports, HSBCe

Valuation and risks

Raise target price from USD27 to USD33; Maintain Buy. We change our valuation methodology from DCF to a sum-of-the-parts in order to better reflect the last round valuation of Yixin Capital (see below for details). Given that 1) Yixin Capital has accounted for a large proportion of Bitauto's valuation, and 2) Yixin's valuation varied from time to time with progress in fundraising, we believe it is more reasonable to value Yixin on standalone basis and use a sum-of-the-parts methodology to value Bitauto.

Our sum-of-the-parts valuation is based on: (1) Yixin Capital: According to company management, Yixin's valuation in the last round fundraising will be around USD3.5-4.0bn (the deal is expected to close by May 2017). Upon completion, Bitauto will still hold no less than 48% of Yixin's outstanding share capital. We conservatively assume Yixin's valuation to be USD3.5bn and Bitauto's stake to be 48%, implying Bitauto's stake of Yixin will be valued at USD1.68bn. (2) Traditional: We estimate 2017 net profit of the traditional business (excluded user-car related business) at cRMB3bn. We apply a 10x forward PE to this business, as we expect the business to grow at a high-single digit CAGR. Thus the traditional part will be valued at USD486m. Combined, we estimate Bitauto equity value at USD2,166m, or USD33 per ADS. Our new TP implies upside of 6.1% and we rate the stock Buy, as we believe the fast progress in platform strategy in Yixin Capital may further improve the company fundamentals in the future. An IPO of Yixin Capital could be a potential future catalyst in our view.

Sum-of-the-part valuation

1) Yixin Capital part	
Valuation (USDm)	3,500
Bitauto's stake	48%
48% stake in Yixin Capital (USDm)	1,680
2) Traditional business part	
2017e net profit (USDm)	49
PE	10x
Traditional part value (USDm)	486
Sum-of-the-parts (USDm)	2,166
Numbers of share (m)	65
Target price (USDm)	33

Source: Company reports, HSBCe

Previously, we used DCF valuation (a 2.5% risk-free rate, a 2.6 equity beta from Bloomberg, a 6% equity risk premium, a WACC of 18.1% and a 2% terminal growth rate) to derive the target price of the stock.

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 the long term. 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.

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

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Hold	40%	(26% of these provided with Investment Banking Services)
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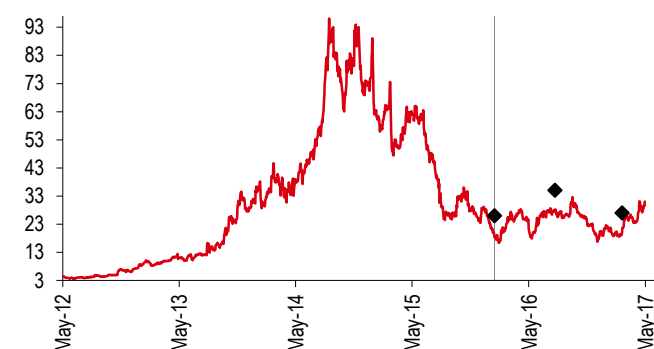
For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

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Share price and rating changes for long-term investment opportunities

Bitauto Holdings (BITA.N) share price performance USD

Vs HSBC rating history



Source: HSBC

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
Price 3	27.00	02 Mar 2017	Terry Chen

Source: HSBC

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Source: HSBC

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