



Rating
Buy

Asia
China

Consumer
Retail / Wholesale Trade

Company
Gree

Reuters 000651.SZ Bloomberg 000651 CH Exchange SHZ Ticker 000651

Date
25 September 2017

Company Update

Price at 25 Sep 2017 (CNY)	38.93
Price target - 12mth (CNY)	44.40
52-week range (CNY)	41.53 - 21.51
Shenzhen Index	2,080

Upstream investments to further enhance its supply chain capability

Event 1 - Clarification of potential investment in Luoyang LYC and Tianjin FAW

On 19 Sep 2017, Gree confirmed it had teamed up with Luoyang Local Government and IIT Committee of Henan province, to participate in the “Luoyang intelligent equipment manufacturing production base project”, reported by the press on 15 Sep 2017. Total investment of this project is around RMB15bn including a site area of 5000mu, and the estimated production value will reach RMB30bn per annum after completion. Gree will also participate in the state-owned enterprise Reform of LYC Bearing; the investment amount from Gree has yet to be defined. The company will make a further announcement if necessary.

Meanwhile, Gree denied it intended to acquire Tianjin FAW Xiali as Souhu.com reported on 16 Sep 2017. Gree clarified that it has never discussed the acquisition of Xiali with Tianjin FAW.

Event 2 - Acquisition of 5% stake in Shanghai Highly Group

Gree resumed trading on 19 Sep and announced on 20 Sep 2017 that it had successfully bid for 43m shares of Shanghai Highly Group (600619.SS, NR) between 29 Aug 2017 and 19 Sep 2017 from its controlling shareholder, Shanghai Electric Group (601727.SS, NR). Following the purchase, Gree owns a 5% stake in Shanghai Highly.

Rationale for the purchase – to be an international company with well-rounded supply chain capability. Through this acquisition, Gree targets to expand its supply chain base and consolidate quality capacity and resources in the market. It will also leverage on its international vision as a Shanghai company, on human resources, information and innovation.

It also mentioned the possibility of increasing its stake in Shanghai Highly in the next 12 months, although it does not intend to be the controlling shareholder of Highly at the moment. It stated that: 1) it will not sell the purchased shares in the next 12 months; 2) it will continue to participate in the bidding for Highly’s shares in the next 12 months should Highly’s controlling shareholder, Shanghai Electric, plan to sell its stake in Highly.

Deutsche Bank view – maintaining Buy

We believe that business diversification remains as one of the key strategies for Gree, and is in line with what it mentioned in its 2016 annual report. Automation in the manufacturing process is one of the focuses for all upstream players. In

Valuation & Risks

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Price/price relative



Performance (%)	1m	3m	12m
Absolute	-1.8	-2.7	81.6
Shenzhen Index	4.1	6.3	-1.0

Source: Deutsche Bank

Key indicators (FY1)

ROE (%)	35.5
Net debt/equity (%)	-178.2
Book value/share (CNY)	10.32
Price/book (x)	3.8
Net interest cover (x)	-
Operating profit margin (%)	16.2

Source: Deutsche Bank



1H17, Gree's manufacturing equipment business sales grew by 270%. As the investment of RMB15bn will be contributed by various partners, we believe Gree's investment in Luoyang LYC can be funded from internal resources and will not affect Gree's cashflow or dividend payout. To recap, as of end-2016, Gree has net cash of RMB84bn including net working capital. In 2016, its dividend payout ratio was 59%.

Gree bought its interest in Highly at a price of RMB11.6-15.5/share (within Highly's trading range during the period), which indicates Gree's total investment into Highly is around RMB556-578m. The consideration implies a 2016 PE of 63-66x, EV/EBITDA of 11~12x, PB of 2.8-2.9x. The impact on the P&L should be very minimal, in our view. The reason for this acquisition is mainly to vertically integrate its supply chain, as explained by Gree. Shanghai Highly is the leading compressor manufacturer in China with a 31.4% share of non-self-supporting compressors in 1H17, according to Highly's interim report. As the largest client for Highly, Gree purchased 6m sets of compressors from Highly (total production of 25m sets) in 2016. Other air conditioners, e.g., Midea and Haier, are all clients of Highly. Gree also owns a compressor manufacturer, i.e., Zhuhai Landa, a subsidiary of Gree. We believe the investment in Highly will further secure Gree's compressor supply and help it to gain market share and strengthen its dominant position in the air-conditioner market, particularly in a high demand market.

Forecasts and ratios

Year End Dec 31	2015A	2016A	2017E	2018E	2019E
Sales (CNYm)	99,812.6	108,682.7	139,979.7	155,684.2	171,216.9
EBITDA (CNYm)	14,315.1	15,515.4	24,349.0	25,866.2	28,495.9
Reported NPAT (CNYm)	12,532.4	15,421.0	20,569.0	22,163.2	24,638.1
Reported EPS FD(CNY)	2.08	2.56	3.42	3.68	4.10
DB EPS FD(CNY)	2.08	2.56	3.42	3.68	4.10
DB EPS growth (%)	-11.5	23.0	33.4	7.8	11.2
PER (x)	10.3	8.3	11.4	10.6	9.5
EV/EBITDA (x)	2.7	2.3	4.7	3.7	2.7
DPS (net) (CNY)	1.50	1.50	2.05	2.21	2.46
Yield (net) (%)	7.0	7.1	5.3	5.7	6.3

Source: Deutsche Bank estimates, company data



Appendix 1

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*Other information available upon request

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Company	Ticker	Recent price*	Disclosure
Gree	000651.SZ	38.93 (CNY) 25 Sep 2017	14

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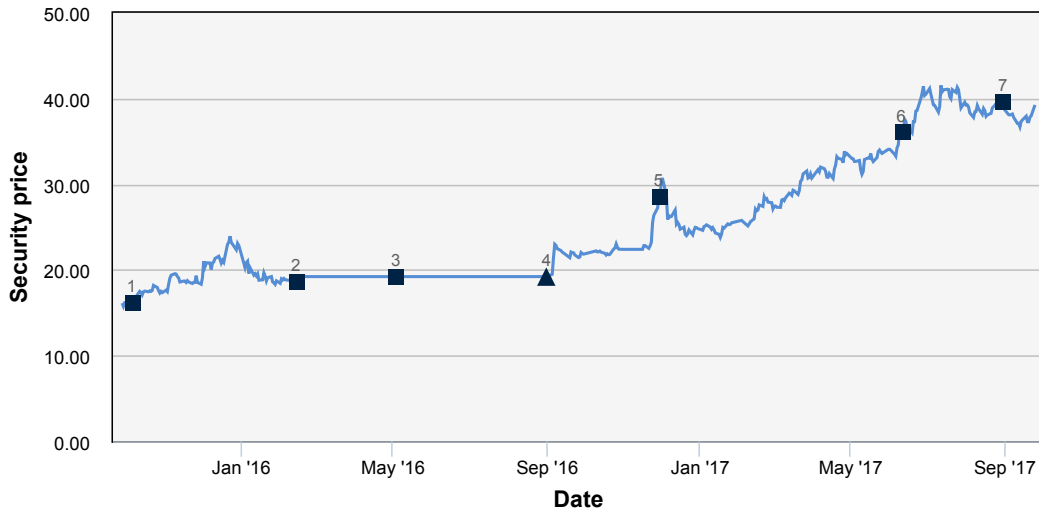
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Historical recommendations and target price. Gree (000651.SZ)

(as of 09/25/2017)



Current Recommendations

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

** Analyst is no longer at Deutsche Bank

1.	10/07/2015	Hold, Target Price Change CNY 17,27	Richard Rui-Huang**	5.	11/30/2016	Buy, Target Price Change CNY 28,48	Richard Rui-Huang**
2.	02/15/2016	Hold, Target Price Change CNY 16,29	Richard Rui-Huang**	6.	06/12/2017	Buy, Target Price Change CNY 38,87	Anne Ling
3.	05/04/2016	Hold, Target Price Change CNY 18,10	Richard Rui-Huang**	7.	08/31/2017	Buy, Target Price Change CNY 44,40	Anne Ling
4.	09/01/2016	Upgraded to Buy, Target Price Change CNY 24,91	Richard Rui-Huang**				

Equity Rating Key

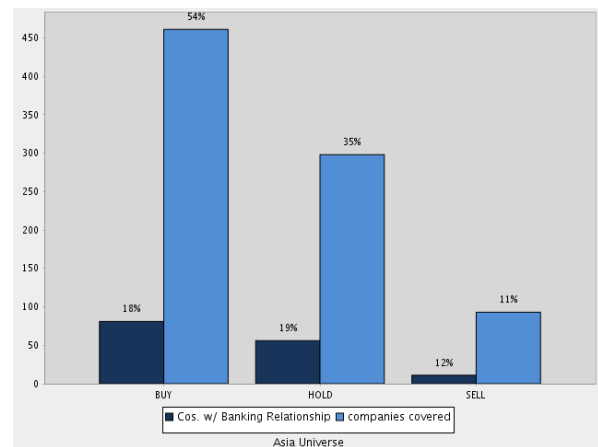
Buy: Based on a current 12- month view of total share-holder return (TSR = percentage change in share price from current price to projected target price plus projected dividend yield) , we recommend that investors buy the stock.

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.

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