Deutsche Bank
Research

Rating
Buy

Asia
China

Automobiles & Components

Company
Yutong Bus

Reuters	Bloomberg	Exchange	Ticker
600066.SS	600066 CH	SHH	600066

Date
28 August 2018

Forecast Change

Price at 27 Aug 2018 (CNY)	15.52
Price target - 12mth (CNY)	22.60
52-week range (CNY)	26.74 - 14.90
Shanghai Composite	2,781

1H18 earnings hurt by subsidy cuts

3.5ppt YoY gross profit margin erosion leading to 23% YoY earnings drop

Yutong announced on 27 August that its 1H18 net profit dropped 23.4% YoY to RMB616.5m. As this accounts for only 16% of our previous FY18 estimates, we consider the results a miss. 1H18 gross revenue grew 29.0% YoY to RMB12.0bn on the back of a 13.5% YoY rise in bus sales volume and increased new energy bus mix. Yet with the effect of new energy vehicle (NEV) subsidy cut, Yutong's 1H18 gross profit margin contracted 3.5ppts YoY to 20.9%. In addition, SG&A also grew at a faster pace than topline growth. As a result, SG&A expense ratio climbed to 16.1% (vs. 14.9% in 1H17).

The company hosted a conference call today. Key takeaways are as follows:

- Profit decline: management attributed the profit decline to the rise in R&D expense and changes in the NEV subsidy policy. To elaborate, the 30% YoY subsidy cut was applied during the transition period (between 12 February 2018 to 11 June 2018). Post 11 June, a 40% YoY cut was applied, which had a negative impact on the company's earnings.
- Sales volume: 1H18 sales volume increased by 13.5% YoY to 24,780 units, with sales volume of new energy bus up 195.7% to 8,765 units and traditional bus down 15.0% YoY to 16,015 units. In terms of breakdown by region, the domestic market rose 24.3% YoY to 21,721 units, whilst overseas markets were under pressure, down 29.8% YoY to 3,059 units.
- Cost cutting: Despite the challenging margin profile in 1H18, the company expects gross profit margin to gradually recover on the back of: 1) improved pricing of new products; 2) better cost control as purchase costs of battery/electric motor/electronic control unit have declined; and 3) increased sales volume, which would lead to lower unit fixed costs.
- Guidance: The company maintains its FY18 target – sales volumes returns to 2016 levels; revenue to reach c.RMB34bn; net profit to maintain at the 2017 level.

Deutsche Bank view – still a well positioned new energy bus manufacturer

On the back of the strong 1H18 topline growth and thus higher ASP assumptions, we raise our FY18-20 revenue forecast by 6.3-6.6% on higher ASP assumptions. On the other hand, with Yutong's weaker-than-expected capability to cut cost

Valuation & Risks

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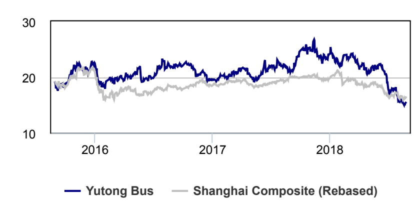
Key changes

TP	25.75 to 22.60	↓	-12.2%
Sales (FYE)	34,801 to 36,992	↑	6.3%
Op prof margin (FYE)	13.1 to 10.0	↓	-23.7%
Net profit (FYE)	3,802.6 to 3,237.6	↓	-14.9%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	-9.1	-28.0	-25.8
Shanghai Composite	-3.2	-11.5	-16.5

Source: Deutsche Bank

Key indicators (FY1)

ROE (%)	19.5
Net debt/equity (%)	-20.6
Book value/share (CNY)	7.96
Price/book (x)	1.9
Net interest cover (x)	21.4
Operating profit margin (%)	10.0

Source: Deutsche Bank

and mitigate subsidy cut pressure, as well as higher SG&A expense estimate on higher R&D, we cut our FY18-20 forecast by 14.3-14.9%.

We still like Yutong's established market position in the bus segment, including the new energy bus segment, and believe its earnings outlook should improve with long-term receding of subsidy cut impacts. Our target price is based on 15.0x FY18/19E P/E (from 15.0x FY18E), about 35% more than Yutong's mid-cycle P/E of 11x to reflect our optimism on Yutong's increased profit contribution from the new energy bus segment. This is justifiable, in our view, as we expect the company to deliver a 11% three-year earnings CAGR in FY17-20E. Key downside risks for Yutong include: 1) unexpected changes in the Chinese government's new energy bus subsidy policy; 2) weaker-than-expected new energy bus demand; and 3) market share loss in new energy buses.

Figure 1: Yutong Bus - summary of forecast changes

	2018E			2019E			2020E		
	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
Sales volume (units)	72,636	72,636	0.0%	79,059	79,059	0.0%	86,642	86,642	0.0%
- ICE bus	41,555	41,555	0.0%	41,139	41,139	0.0%	41,139	41,139	0.0%
- NEV bus	31,081	31,081	0.0%	37,919	37,919	0.0%	45,503	45,503	0.0%
Revenue (RMBm)	34,996.1	37,199.7	6.3%	38,060.9	40,614.9	6.7%	42,693.8	45,498.1	6.6%
Gross profit (RMBm)	9,140.5	9,030.3	-1.2%	10,114.8	10,046.9	-0.7%	11,427.8	11,340.8	-0.8%
Gross profit margin	26.3%	24.4%		26.7%	24.9%		26.9%	25.1%	
Net profit (RMBm)	3,802.6	3,237.6	-14.9%	4,319.3	3,693.2	-14.5%	4,942.8	4,236.8	-14.3%
Net profit margin	10.9%	8.8%		11.4%	9.1%		11.6%	9.4%	

Source: Deutscxhe Bank estimate

Forecasts and ratios

Year End Dec 31	2016A	2017A	2018E	2019E	2020E
Sales (CNYm)	35,689.1	33,036.3	36,991.9	40,387.9	45,243.9
EBITDA (CNYm)	5,774.6	4,864.3	4,417.4	5,032.3	5,718.6
Reported NPAT (CNYm)	4,043.7	3,129.2	3,237.6	3,693.2	4,236.8
Reported EPS FD (CNY)	1.83	1.41	1.46	1.67	1.91
DB EPS FD (CNY)	1.71	1.27	1.40	1.61	1.86
OLD DB EPS FD (CNY)	1.71	1.27	1.64	1.88	2.17
% Change	0.0%	0.0%	-14.6%	-14.5%	-14.4%
DB EPS growth (%)	16.3	-25.8	10.8	14.9	15.4
PER (x)	12.1	17.3	11.1	9.6	8.3
EV/EBITDA (x)	6.6	9.2	6.5	5.4	4.5
DPS (net) (CNY)	1.00	0.50	0.51	0.58	0.67
Yield (net) (%)	4.9	2.3	3.3	3.8	4.3

Source: Deutsche Bank estimates, company data

Appendix 1

Important Disclosures

*Other information available upon request

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Company	Ticker	Recent price*	Disclosure
Yutong Bus	600066.SS	15.52 (CNY) 27 Aug 2018	14

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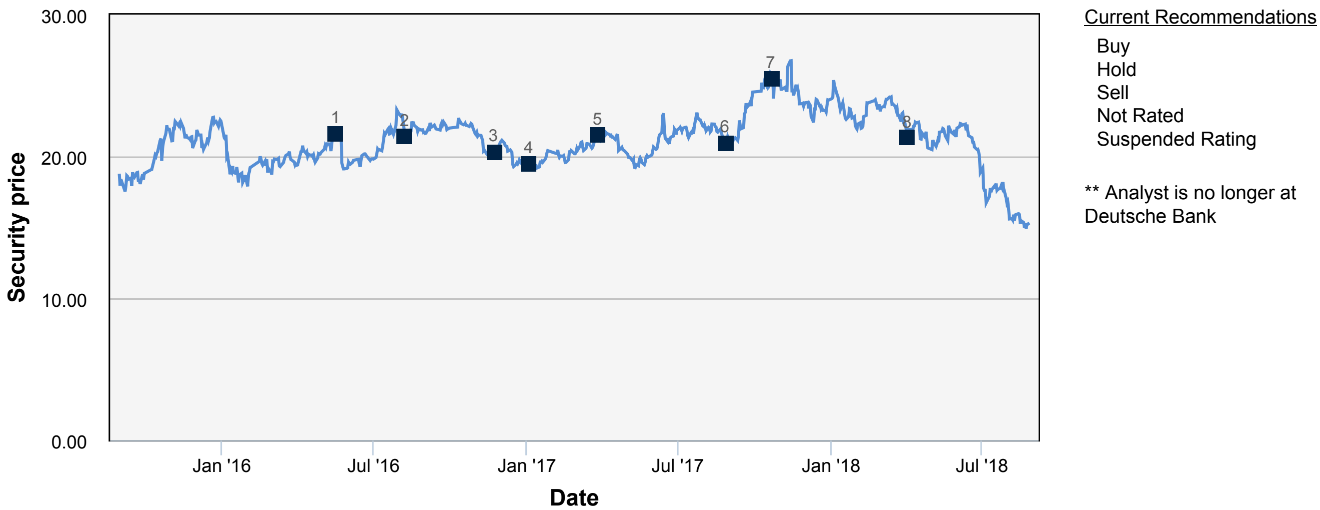
Historical recommendations and target price. Yutong Bus (600066.SS)

(as of 08/27/2018)



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2.	08/08/2016	Buy, Target Price Change CNY 24.90 Vincent Ha, CFA
3.	11/24/2016	Buy, Target Price Change CNY 24.00 Vincent Ha, CFA
4.	01/04/2017	Buy, Target Price Change CNY 22.60 Fei Sun, CFA**
5.	03/28/2017	Buy, Target Price Change CNY 24.00 Fei Sun, CFA**
6.	08/28/2017	Buy, Target Price Change CNY 25.20 Fei Sun, CFA**
7.	10/23/2017	Buy, Target Price Change CNY 26.60 Fei Sun, CFA**
8.	04/03/2018	Buy, Target Price Change CNY 25.75 Vincent Ha, CFA

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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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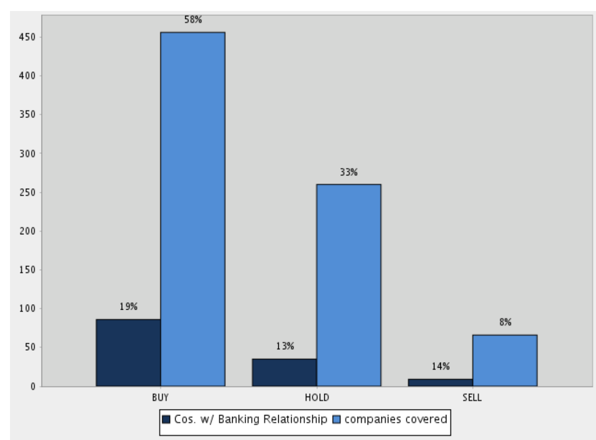

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