

GAC Group (2238 HK)

3Q20 performance update

GAC Group announced its 3Q20 results. In the first three quarters of 2020, top-line achieved RMB43.2bn, an increase of 0.3% YoY while NP was RMB5.0bn, a decrease of 21% YoY. In 3Q20, top-line was RMB17.5bn, an increase of 19% YoY while NP was RMB2.7bn, an increase of 90% YoY. 3Q20 performance beat market estimation. We raise our TP to HK\$12.1 (based on 15.0x 2021E P/E) with an upside of 52.8% from initial TP HK\$10.0 (based on initial 16.0x average 2020E/21E P/E). Reiterate BUY.

■ **In 3Q20, GAC achieved total sales of 98,860 units, an increase of 10% YoY.** Unit revenue increased by 9% YoY, which led to a 19% YoY growth in top-line. GPM was 5.2%, down 0.8ppt YoY/1.5ppt QoQ. Exp ratio achieved a YoY decline thanks to strong cost control measures (S&D ratio -1.3ppt YoY, Admin ratio -1.5ppt YoY, R&D ratio -1.2ppt YoY). Due to top-line growth and expense saving, 3Q20 core profit (loss) narrowed by 13% YoY. Benefiting from the rapid sales growth of GAC Honda (+29% YoY) and GAC Toyota (+20% YoY) in 3Q20, investment income from JVs and associates in 3Q20 achieved RMB3.4bn, an increase of 35% YoY. We expect that GAC Group's sales and NP in the 4Q20E will continue to deliver rapid growth.

■ **Even though GACM is undergoing a 3-year transition period, sales volume has begun to recover after its new flagship model GS4 rollout at the end of 2019.** Especially GS4 has achieved a monthly sales volume more than 10K units for the last five consecutive months. We expect that the launch of GS3 Power will continue to drive the recovery of GACM. MPV series (M6 and M8) have earned good market awareness, with an increase of 36% YoY in Sep. The new model pipeline includes a new A+ sports sedan and the brand new GS8 model in 2021E. We believe GACM will bottom out as intelligent technologies (AGIDO 3.0) are gradually installed in its new models. We expect GAC Trumpchi to achieve a 6% sales growth in 4Q20E.

■ **We raise our bottom-line forecast to RMB5.9bn in 2020E to reflect the strong 3Q20 result.** Our revised NP forecast suggests that GWM's bottom-line will grow 191% YoY in 4Q20E. At the same time, we revised up our NP forecast to RMB7.3bn in 2021E to reflect a more positive forecast on GACM. We raise our TP to HK\$12.1 (based on 15.0x 2021E P/E) with an upside of 52.8% from initial TP HK\$10.0 (based on initial 16.0x average 2020E/21E P/E). Reiterate BUY.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	72,380	59,704	61,521	66,009	69,751
YoY growth (%)	1.12%	-17.51%	3.04%	7.30%	5.67%
Net income (RMB mn)	10,900	6,616	5,825	7,271	8,433
EPS (RMB)	1.07	0.65	0.57	0.71	0.82
YoY growth (%)	-29%	-39%	-12%	25%	16%
Consensus EPS(RMB)	NA	NA	0.65	0.85	0.97
P/E (x)	6.55	10.79	12.25	9.82	8.46
P/B (x)	0.92	0.87	0.82	0.78	0.73
Yield (%)	5.30%	2.87%	2.48%	3.10%	3.59%
ROE (%)	14.93%	8.44%	7.08%	8.37%	9.12%
Net gearing (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

Target Price	HK\$12.1
(Previous TP)	HK\$10.0
Up/Downside	+52.8%
Current Price	HK\$8.0

China Auto Sector

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Stock Data

Mkt Cap (HK\$ mn)	135,195
Avg 3 mths t/o (HK\$ mn)	220.35
52w High/Low (HK\$)	9.85/5.48
Equity share – 2238.HK	3,099
Equity share - 601238.SH	7,139

Source: Wind

Shareholding Structure

Guangzhou Automobile Industry Group Co., Ltd	72.96%
Brown Brothers Harriman & Co.	7.23%
AEGON-Industrial Fund	5.90%

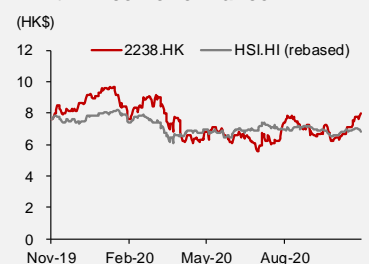
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	23.3%	19.9%
3-mth	9.8%	12.5%
6-mth	17.1%	19.7%

Source: Wind

12-mth Price Performance



Source: Wind

Auditor: PricewaterhouseCoopers

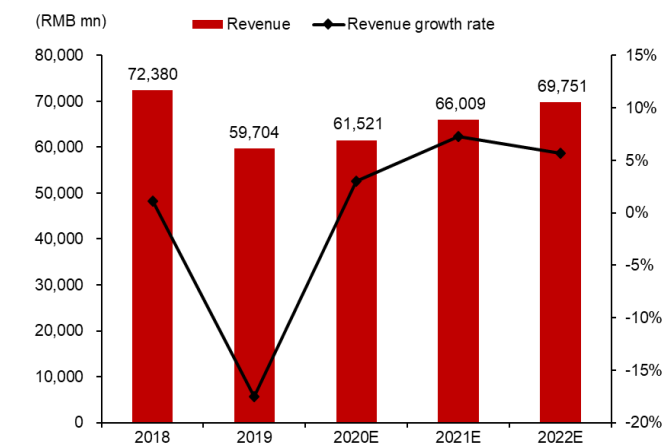
Related Reports

- "GAC Group (2238 HK) – Several catalysts support the valuation lift" – 2 Sep 2020
- "GAC Group (2238 HK) – Expect earnings rebound from 2Q20E" – 4 May 2020
- "GAC Group (2238 HK) – Promising performance after the epidemic" – 26 Feb 2020

- **Toyota will provide hybrid technology to GAC Group.** The latest version of "Energy-saving and New Energy Vehicle Technology Roadmap 2.0" encourages hybrid development, and specifically proposes the development of HEV (different from the traditional BEV/48V/PHEV/FCV classification). Among the HEV technologies, the Japanese brand, namely Toyota and Honda, has the strongest technical accumulation and is especially known for its fuel economy. We expected that GACM will take advantage of technological cooperation to further boost its GACM brands. Accelerating the introduction of related HEV models will also help alleviate the market's concerns about double-credit regulation as the double-credit regulation will be strictly enforced since 2021E. For Toyota, promoting hybrid technology with its Chinese partners can form a scale effect and amortize the relevant cost.
- **GAC NEV sold 7,006 units in Sep, an increase of 75% YoY.** Cumulative sales from Jan to Sep 2020 were 38,000 units, an increase of 75% YoY. Among them, the Aion series sold 6,875 units in Sep, up 72% YoY. From the perspective of product competitiveness, the first-generation Aion series has a good reputation among NEV customers. We expect GAC NEV will launch a variety of models in the future to enrich the product matrix based on its third-generation BEV platform of GEP3.0. The profitability of GAC NEV has gradually improved given 1) economies of scale brought by sales growth and 2) battery cost control given the introduction of new battery supplier CALB. Market is speculating the Aion will operate independently in Nov and will form two major brands of Aion and Trumpchi under GACG. At present, the capital market poses higher valuations for NEV than ICE. For GAC Group, the independent GAC NEV will help the capital market re-price its NEV segment and raise the overall valuation of the GAC Group.

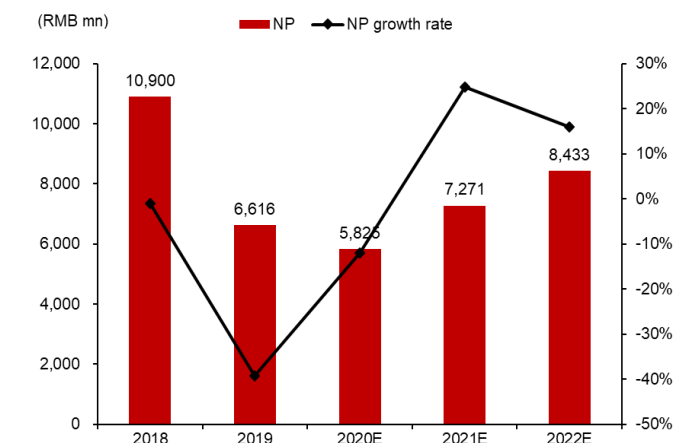
Focus chart

Figure 1: Revenue forecast



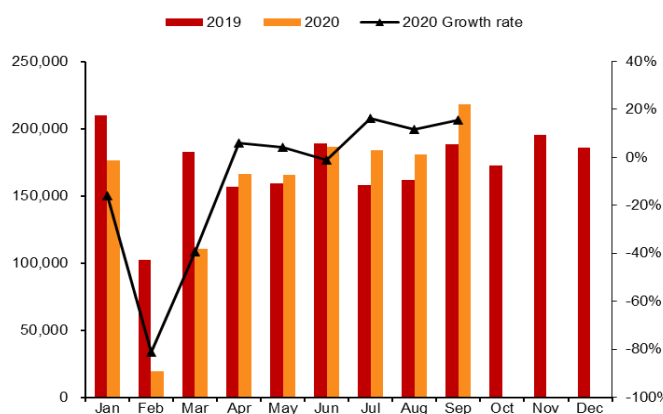
Source: Company data, CMBIS estimates

Figure 2: Bottom-line forecast



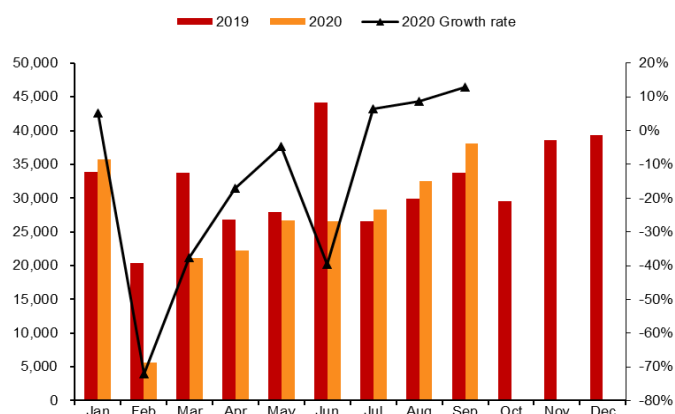
Source: Company data, CMBIS estimates

Figure 3: GAC Group sales volume



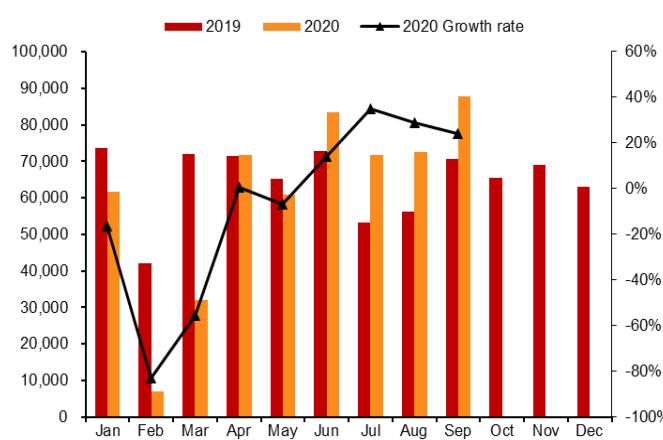
Source: Company data, CMBIS

Figure 4: GACM sales volume



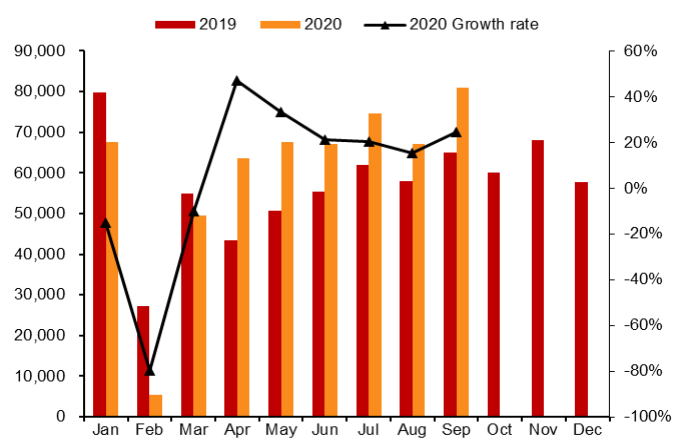
Source: Company data, CMBIS

Figure 5: GAC Toyota sales volume



Source: Company data, CMBIS

Figure 6: GAC Honda sales volume



Source: Company data, CMBIS

Earnings Revision

Figure 7: Earnings revision

(RMB mn)	New		Old		Change (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Revenue	61,521	66,009	61,864	65,595	-1%	1%
Gross profit	3,356	3,977	2,291	3,632	46%	10%
Net profit	5,825	7,271	4,689	6,530	24%	11%
EPS (RMB)	0.57	0.71	0.46	0.64	24%	11%
Gross margin	5.46%	6.03%	3.70%	5.54%	1.8 ppt	0.5 ppt
Net Margin	9.47%	11.02%	7.58%	9.96%	1.9 ppt	1.1 ppt

Source: Company data, CMBIS estimates

Figure 8: CMBIS estimates vs consensus

(RMB mn)	CMBIS		Consensus		Diff (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Revenue	61,521	66,009	56,814	63,661	8%	4%
Gross profit	3,356	3,977	3,499	5,067	-4%	-22%
Net profit	5,825	7,271	6,681	8,723	-13%	-17%
EPS (RMB)	0.57	0.71	0.65	0.85	-13%	-17%
Gross margin	5.46%	6.03%	6.16%	7.96%	-0.7 ppt	-1.9 ppt
Net Margin	9.47%	11.02%	11.67%	13.65%	-2.2 ppt	-2.6 ppt

Source: Bloomberg, CMBIS estimates

Figure 9: P&L forecast

(RMB mn)	FY18	FY19	FY20E	FY21E	FY22E
Revenue	72,380	59,704	61,521	66,009	69,751
...YoY	1.12%	-17.51%	3.04%	7.30%	5.67%
Cost of sales	(60,836)	(57,181)	(58,165)	(62,032)	(65,282)
Gross profit	11,544	2,523	3,356	3,977	4,469
GPM (%)	15.95%	4.23%	5.46%	6.03%	6.41%
...YoY	-10.23%	-78.14%	33.02%	18.50%	12.35%
Selling Exp	(5,073)	(4,553)	(4,583)	(4,918)	(5,196)
...% of rev	-7.01%	-7.63%	-7.45%	-7.45%	-7.45%
Admin Exp	(4,519)	(3,590)	(3,568)	(3,763)	(3,941)
...% of rev	-6.24%	-6.01%	-5.80%	-5.70%	-5.65%
Operating profit	3,466	(2,763)	(3,011)	(3,115)	(3,081)
OPM (%)	4.79%	-4.63%	-4.90%	-4.72%	-4.42%
...YoY	-22.84%	-179.72%	8.99%	3.44%	-1.10%
Net profit	10,900	6,616	5,825	7,271	8,433
NPM (%)	15.06%	11.08%	9.47%	11.02%	12.09%
...YoY	-0.95%	-39.30%	-11.95%	24.82%	15.98%

Source: Company data, CMBIS estimates

Figure 10: Revenue breakdown

(RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Automobile manufacturing industry	50,394	36,060	36,471	38,546	39,527
...YoY	0%	-28%	1%	6%	3%
Sedans	5,264	5,473	5,163	5,530	5,585
...YoY	31%	4%	-6%	7%	1%
SUV	42,046	25,078	25,192	26,467	27,261
...YoY	-9%	-40%	0%	5%	3%
MPV	3,083	5,510	6,116	6,550	6,681
...YoY	5578%	79%	11%	7%	2%
Auto-parts manufacturing industry	2,882	2,474	2,227	2,338	2,525
...YoY	-1%	-14%	-10%	5%	8%
Commercial services	16,374	18,851	20,736	23,017	25,549
...YoY	0%	15%	10%	11%	11%
Financial services and others	2,730	2,319	2,087	2,108	2,150
...YoY	34%	-15%	-10%	1%	2%
Total	72,380	59,704	61,521	66,009	69,751
...YoY	1%	-18%	3%	7%	6%

Source: Company data, CMBIS estimates

Figure 11: 3Q20 Result summary

	3Q19	3Q20	YoY	First three quarters 19	First three quarters 20	YoY
Revenue	14,680	17,507	19%	43,031	43,149	0%
Cost of sales	(13,806)	(16,596)	20%	(39,450)	(40,726)	3%
Gross profit	874	911	4%	3,581	2,422	-32%
Taxes and levies	(288)	(371)	29%	(968)	(916)	-5%
S&D	(968)	(934)	-4%	(2,703)	(2,364)	-13%
Administrative expenses	(658)	(528)	-20%	(1,956)	(1,953)	0%
R&D expenses	(382)	(246)	-35%	(1,125)	(638)	-43%
Finance expenses	(52)	(113)	118%	(111)	(50)	-55%
Impairment losses on assets	11	3	-73%	0	(41)	-9050%
Impairment losses on credit	15	15	1%	30	15	-50%
Other income	273	460	69%	1,561	772	-51%
Investment income	2,549	3,548	39%	7,509	7,664	2%
PL from JVs	2,530	3,417	35%	7,397	7,404	0%
GL from changes in fair values	21	29	39%	62	100	60%
GL on disposal of subsidiaries	2	(55)	-2609%	4	(51)	-1512%
Operating profit	1,397	2,719	95%	5,884	4,959	-16%
Non-operating income	21	14	-33%	524	48	-91%
Non-operating expenses	(4)	(16)	280%	(18)	(39)	117%
Profit before tax	1,414	2,717	92%	6,390	4,968	-22%
Income tax expense	33	8	-74%	30	101	231%
Profit for the year	1,446	2,726	88%	6,421	5,069	-21%
Non-controlling interests	30	42	40%	86	67	-22%
NP	1,416	2,684	90%	6,335	5,002	-21%

Source: Company data, CMBIS

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	72,380	59,704	61,521	66,009	69,751
Cost of sales	(60,836)	(57,181)	(58,165)	(62,032)	(65,282)
Gross profit	11,544	2,523	3,356	3,977	4,469
Selling & distribution costs	(5,073)	(4,553)	(4,583)	(4,918)	(5,196)
Admin expenses	(4,519)	(3,590)	(3,568)	(3,763)	(3,941)
Impairment loss on financial assets	(7)	(54)	(54)	(54)	(54)
Interest income from time deposits	453	291	300	322	322
Other gains – net	1,068	2,620	1,538	1,320	1,320
Operating profit/(loss)	3,466	(2,763)	(3,011)	(3,115)	(3,081)
Finance costs	(459)	(516)	(628)	(817)	(881)
Interest income from cash	103	172	158	158	158
PL from JV & associates	8,753	9,399	9,765	11,703	13,049
Profit before income tax	11,863	6,292	6,284	7,928	9,245
Income tax expense	(921)	417	(377)	(555)	(693)
Profit for the year	10,942	6,709	5,907	7,373	8,552
Less: MI	43	93	82	102	119
Net Profit	10,900	6,616	5,825	7,271	8,433

Cash flow

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income	10,900	6,616	5,825	7,271	8,433
D&A	3,140	4,184	4,613	5,314	5,957
Change in working capital	(6,263)	9,344	(9,949)	5,705	(5,167)
Others	11,921	(13,179)	4,850	(10,135)	(413)
Net cash from operating	19,698	6,965	5,340	8,155	8,810
Capex & investments	(9,107)	(12,725)	(9,985)	(10,434)	(11,175)
Associated companies	(3,252)	(3,010)	(1,886)	(2,598)	(2,775)
Others	2,319	10,045	3,656	5,999	7,356
Net cash from investing	(10,040)	(5,689)	(8,214)	(7,034)	(6,595)
Equity raised	360	1,116	-	-	-
Change of debts	1,528	2,830	5,650	2,886	1,847
Dividend paid	(3,786)	(2,047)	(1,772)	(2,212)	(2,565)
Others	(4,603)	(1,995)	-	-	-
Net cash from financing	(6,501)	(95)	3,878	674	(719)
Net change in cash	3,157	1,181	1,003	1,795	1,497
Cash at the beginning	39,355	31,572	25,283	26,286	28,082
Exchange difference	(10,940)	(7,469)	-	-	-
Cash at the end	31,572	25,283	26,286	28,082	29,578
Less: pledged cash	3,842	1,678	1,678	1,678	1,678

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	65,963	80,599	88,559	95,087	102,715
Fixed asset	16,318	19,396	21,749	24,059	26,112
Intangible assets	8,540	10,810	13,015	15,055	16,983
Interest in JV /associates	28,995	32,005	33,891	36,488	39,264
Other non-current assets	12,109	18,388	19,905	19,485	20,355
Current assets	66,211	56,865	62,359	60,828	63,424
Cash	31,572	25,283	26,286	28,082	29,578
Account receivable	16,605	16,844	20,507	17,371	18,355
Inventory	6,730	6,928	7,755	7,565	7,680
Other current assets	11,304	7,810	7,810	7,810	7,810
Current liabilities	40,291	41,776	52,139	51,981	55,185
Borrowings	2,829	6,347	11,570	13,774	15,052
Account payables	35,786	33,616	38,776	36,490	38,401
Other payables	1,336	1,529	1,529	1,529	1,529
Tax payables	340	284	263	189	203
Non-current liabilities	13,908	13,180	12,135	12,129	13,162
Borrowings	9,611	8,924	9,351	10,033	10,602
Provisions	675	1,015	923	990	1,046
Deferred income tax	161	183	75	111	139
Others	3,461	3,058	1,786	994	1,375
Shareholders' equity	76,604	80,188	84,324	89,485	95,471
Minority Interest	1,371	2,320	2,320	2,320	2,320
Total net assets	77,975	82,508	86,644	91,805	97,791

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Automobile manufacturing	70%	60%	59%	58%	57%
Auto-parts manufacturing	4%	4%	4%	4%	4%
Commercial services	23%	32%	34%	35%	37%
Financial services	4%	4%	3%	3%	3%
Total	100%	100%	100%	100%	100%
P&L ratios (%)					
Gross profit margin	16%	4%	5%	6%	6%
Pre-tax margin	16%	11%	10%	12%	13%
Net margin	15%	11%	9%	11%	12%
Effective tax rate	8%	-7%	6%	7%	8%
Balance sheet ratios					
Current ratio (x)	1.64	1.36	1.20	1.17	1.15
Quick ratio (x)	1.48	1.20	1.05	1.02	1.01
Cash ratio (x)	0.78	0.61	0.50	0.54	0.54
Debtors turnover days	4.36	3.54	3.00	3.80	3.80
Total debt/ total equity ratio (%)	70%	67%	74%	70%	70%
Net debt/ equity ratio (%)	net cash	net cash	net cash	net cash	net cash
Returns (%)					
ROE	15%	8%	7%	8%	9%
ROA	10%	5%	5%	6%	6%
Per share					
EPS (RMB)	1.07	0.65	0.57	0.71	0.82
DPS (RMB)	0.37	0.20	0.17	0.22	0.25
BVPS (RMB)	7.62	8.06	8.46	8.97	9.55

Source: Company data, CMBIS estimates

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