

China Meidong Auto (1268 HK)

Lingering industry headwinds amid high valuation

We **downgrade Meidong to HOLD** from Buy despite its superb management execution, as we believe it still faces strong industry headwinds in the short term and may lack catalysts amid its high valuation. We think the weak earnings in 2H22 could extend into 1H23E.

- **Key metrics in 2H22 trailing peers.** Porsche's new-car GPM at Meidong narrowed to a historical-low of 3.2% in 2H22. Its BMW new-car GPM in 2H22 also fell to a multi-year low of -0.3%. Both figures were significantly lower than its peers, which was rare in history. Although it coincided with strong industry headwinds in 2H22, it appears to us that StarChase's turnaround was far below our prior expectation.
- **Investors may underestimate the lingering effect of industry headwinds.** The dent on profitability from the 4Q22 weakness did not end last year, as a large portion of low-margin orders in 4Q22 were delivered in 1Q23. The lower-than-expected recovery, along with fierce price war in 1Q23 could also lead to continued margin weakness in 2Q23. Management mentioned that the current new-car GPMs were about 70%, 60% and 50% of the last year's average for Porsche, BMW and Lexus, respectively.
- **We cut FY23E net profit by 31%.** We project new-car and after-sales service revenue to rise 13% YoY and 26% YoY in FY23E, respectively, mainly driven by Porsche (assuming new-car sales of 16,000 units in FY23E). We expect new-car GPM to widen from 3.4% in FY22 to 4.1% in FY23E, assuming such GPM to double in 2H23E from 1H23E, although the visibility is still low now.
- **Long-term uncertainties may cap valuation.** Unlike 2017-20 when traditional luxury cars significantly outperformed China's overall auto sales growth, competition from EVs has been apparent and would continue. Although we believe dealers will exist in the long term, traditional luxury brands' prolonged EV transformation could hurt their dealers' profitability even if these brands survive in the EV world. That could cap Meidong's valuation, as Meidong's superb execution capabilities could help it outrun its peers even if it starts late, but could not help it stay away from industry headwinds.
- **Valuation/Key risks.** We cut our target price from HK\$ 25.00 to HK\$ 17.00, still based on 20x of our revised FY23E EPS (FY23E NP of RMB 1.0bn). We are of the view that such valuation is fair given the significant premium to its peers (4-10x FY23E P/E) and long-term uncertainties amid industry revolution. Key risks to our rating and target price include higher/lower sales and/or margins, as well as a sector re-rating or de-rating.

Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22A	FY23E	FY24E
Revenue (RMB mn)	20,207	23,577	28,655	32,846	36,557
YoY growth (%)	30.7	36.1	(9.1)	29.4	25.2
Net income (RMB mn)	751	1,166	521	1,014	1,536
EPS (RMB)	0.61	0.92	0.41	0.75	1.12
YoY growth (%)	36.3	55.3	(55.3)	94.5	51.5
P/E (x)	22.9	14.7	36.6	19.7	13.1
P/B (x)	5.5	4.4	4.5	3.4	2.8
Yield (%)	2.1	2.6	1.0	2.5	3.8
ROE (%)	30.4	32.5	12.7	19.8	23.5
Net gearing (%)	Net cash	Net cash	20.8	Net cash	Net cash

Source: Company data, Bloomberg, CMBIGM estimates

HOLD (Down)

Target Price	HK\$ 17.00
(Previous TP	HK\$ 25.00)
Up/Downside	+0.4%
Current Price	HK\$ 16.94

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Stock Data

Mkt Cap (HK\$ mn)	22,784
Avg 3 mths t/o (HK\$ mn)	106
52w High/Low (HK\$)	31.45/9.88
Total Issued Shares (mn)	1,345

Source: Bloomberg

Shareholding Structure

Apex Sail Limited	52.2%
Others	47.8%

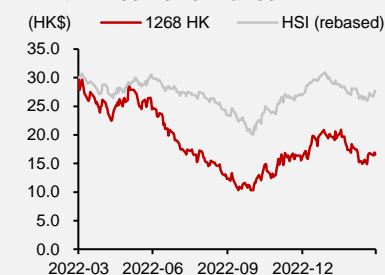
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-8.2%	-7.6%
3-mth	3.5%	0.8%
6-mth	33.5%	15.6%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: KPMG

Related Report

["China Meidong Auto - We expect 2H22E net profit to fall 23% YoY" - 2 Feb 2023](#)

Figure 1: FY22 results review

RMB mn	1H20	2H20	1H21	2H21	1H22	2H22	YoY	HoH
New-car sales volume (units)	23,691	33,509	32,221	29,374	29,658	38,213	30.1%	28.8%
Total revenue	8,448	11,760	11,808	11,769	12,658	15,996	35.9%	26.4%
Gross profit	819	1,216	1,274	1,497	1,334	1,183	-20.9%	-11.3%
Selling exp.	(238)	(308)	(348)	(393)	(398)	(462)	17.5%	16.1%
Admin exp.	(216)	(223)	(278)	(301)	(377)	(433)	44.2%	14.9%
Operating profit	453	693	771	927	668	446	-52.0%	-33.3%
Net profit	301	450	537	629	343	178	-71.7%	-48.2%
Gross margin	9.7%	10.3%	10.8%	12.7%	10.5%	7.4%	-5.3 ppt	-3.1 ppt
Operating margin	5.4%	5.9%	6.5%	7.9%	5.3%	2.8%	-5.1 ppt	-2.5 ppt
Net margin	3.6%	3.8%	4.5%	5.3%	2.7%	1.1%	-4.2 ppt	-1.6 ppt

Source: Company data, CMBIGM estimates

Figure 2: Earnings revision

RMB mn	New			Old			Diff (%)		
	FY22A	FY23E	FY24E	FY22E	FY23E	FY24E	FY22A	FY23E	FY24E
Revenue	28,655	32,846	36,557	29,963	35,422	42,145	-4.4%	-7.3%	-13.3%
Gross Profit	2,517	3,257	4,076	2,910	4,026	5,063	-13.5%	-19.1%	-19.5%
Operating Profit	1,114	1,725	2,480	1,440	2,359	3,169	-22.7%	-26.9%	-21.7%
Net profit	521	1,014	1,536	828	1,460	2,062	-37.1%	-30.6%	-25.5%
Gross Margin	8.8%	9.9%	11.1%	9.7%	11.4%	12.0%	-0.9 ppt	-1.5 ppt	-0.9 ppt
Operating Margin	3.9%	5.3%	6.8%	4.8%	6.7%	7.5%	-0.9 ppt	-1.4 ppt	-0.7 ppt
Net Margin	1.8%	3.1%	4.2%	2.8%	4.1%	4.9%	-0.9 ppt	-1.0 ppt	-0.7 ppt

Source: CMBIGM estimates

Figure 3: CMBI estimates vs consensus

RMB mn	CMBIGM			Consensus			Diff (%)		
	FY22A	FY23E	FY24E	FY22E	FY23E	FY24E	FY22A	FY23E	FY24E
Revenue	28,655	32,846	36,557	28,896	35,985	42,600	-0.8%	-8.7%	-14.2%
Gross Profit	2,517	3,257	4,076	2,955	3,842	4,562	-14.8%	-15.2%	-10.7%
Operating Profit	1,114	1,725	2,480	1,419	2,139	2,645	-21.5%	-19.4%	-6.2%
Net profit	521	1,014	1,536	848	1,393	1,693	-38.6%	-27.2%	-9.3%
Gross Margin	8.8%	9.9%	11.1%	10.2%	10.7%	10.7%	-1.4 ppt	-0.8 ppt	0.4 ppt
Operating Margin	3.9%	5.3%	6.8%	4.9%	5.9%	6.2%	-1.0 ppt	-0.7 ppt	0.6 ppt
Net Margin	1.8%	3.1%	4.2%	2.9%	3.9%	4.0%	-1.1 ppt	-0.8 ppt	0.2 ppt

Source: Bloomberg, CMBIGM estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Revenue	20,207	23,577	28,655	32,846	36,557
Cost of sales	(18,172)	(20,806)	(26,137)	(29,590)	(32,481)
Gross profit	2,035	2,771	2,517	3,257	4,076
Other income	96	247	267	340	384
Distribution expenses	(546)	(741)	(860)	(948)	(1,005)
Administrative expenses	(439)	(578)	(811)	(925)	(975)
Operating profit	1,146	1,698	1,114	1,725	2,480
Finance costs	(137)	(133)	(275)	(290)	(288)
Share of profits of assos	-	-	-	-	-
Share of profits of JVs	43	48	25	30	32
Profit before tax	1,052	1,613	864	1,464	2,224
Taxation	(282)	(399)	(308)	(381)	(578)
Minority interests	(20)	(48)	(35)	(70)	(110)
Net profit	751	1,166	521	1,014	1,536

Cash flow summary

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Profit before taxation	1,052	1,613	864	1,464	2,224
Depreciation/amortization	229	287	490	587	639
Change in working capital	35	276	(209)	358	275
Others	(125)	(364)	9	(175)	(431)
Net cash from operating	1,191	1,812	1,154	2,233	2,706
Capex	(336)	(363)	(283)	(290)	(290)
Others	190	(1,019)	(3,200)	101	(1,955)
Net cash from investing	(145)	(1,382)	(3,483)	(189)	(2,245)
Share issuance	1,166	11	647	946	35
Dividend paid	(420)	(475)	(1,027)	(375)	(671)
Others	(298)	146	1,708	(799)	(113)
Net cash from financing	449	(317)	1,328	(229)	(749)
Net change in cash	1,494	112	(1,002)	1,815	(287)
Cash at beginning of the year	1,124	2,538	2,622	1,636	3,451
Exchange difference	(80)	(29)	16	-	-
Cash at the end of the year	2,538	2,622	1,636	3,451	3,163

Balance sheet

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Current assets	5,110	5,563	5,888	7,792	7,579
Cash and equivalents	2,538	2,622	1,636	3,451	3,163
Accounts receivables	1,518	1,817	1,560	2,250	2,504
Inventories	495	355	1,069	892	712
Other current assets	559	769	1,623	1,200	1,200
Non-current assets	2,661	4,240	8,351	8,330	10,504
PP&E	1,120	1,381	1,843	1,881	2,166
Intangibles	61	546	3,477	3,295	4,612
Interests in JVs and assos	56	62	39	39	42
Other non-current assets	1,423	2,250	2,992	3,116	3,685
Total assets	7,770	9,803	14,239	16,123	18,084
Current liabilities	3,061	4,089	4,874	4,828	5,420
Short-term debt	729	989	1,414	900	1,100
Accounts payable	2,082	2,788	3,193	3,648	4,004
Other current liabilities	250	312	267	280	315
Non-current liabilities	1,365	1,597	4,932	5,160	5,312
Long-term debt	222	299	2,768	2,848	2,711
Other non-current liabilities	1,143	1,297	2,164	2,313	2,602
Total liabilities	4,426	5,686	9,806	9,988	10,732
Share capital	99	100	102	109	110
Reserves	3,127	3,847	4,173	5,845	7,028
Minority interests	118	170	159	180	213
Shareholders' equity	3,227	3,947	4,275	5,955	7,139
Total equity and liabilities	7,770	9,803	14,239	16,123	18,084

Key ratios

YE 31 Dec	FY20A	FY21A	FY22A	FY23E	FY24E
Sales mix (%)					
Sales of new vehicles	88.9	88.3	88.3	87.2	85.6
After-sales services	11.1	11.7	11.7	12.8	14.4
Growth (%)					
Revenue	24.7	16.7	21.5	14.6	11.3
Gross profit	30.7	36.1	(9.1)	29.4	25.2
Operating profit	36.9	48.2	(34.4)	54.9	43.8
Net profit	36.3	55.3	(55.3)	94.5	51.5
Profit & loss ratio (%)					
Gross margin	10.1	11.8	8.8	9.9	11.1
Operating margin	5.7	7.2	3.9	5.3	6.8
Net profit margin	3.7	4.9	1.8	3.1	4.2
Balance sheet ratio					
Net cash/total equity (x)	0.6	0.5	(0.2)	0.1	0.1
Current ratio (x)	1.7	1.4	1.2	1.6	1.4
Receivable turnover days	27.4	28.1	19.9	25.0	25.0
Inventory turnover days	9.9	6.2	14.9	11.0	8.0
Payable turnover days	41.8	48.9	44.6	45.0	45.0
Profitability (%)					
ROE	30.4	32.5	12.7	19.8	23.5
ROA	11.0	13.3	4.3	6.7	9.0
Per share data (RMB)					
EPS	0.61	0.92	0.41	0.75	1.12
DPS	0.39	0.83	0.20	0.37	0.56

Source: Company data, CMBIGM estimates

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