

# MeiDong Auto(1268 HK)

## High future growth underpins the valuation

**MeiDong released its 1H20 results.** 1H20 top-line increased by 23% YoY to RMB8.4bn, among which revenue from new car sales increased by 24% YoY to RMB7.5bn while revenue from after-sales service increased by 16% YoY to RMB960mn. 1H20 bottom-line increased by 28% YoY to RMB301mn. The Company declared an interim dividend of RMB0.15 per share, representing a 60% payout ratio.

- MeiDong delivered outstanding results in 1H20.** Despite the negative impact of COVID-19, new car sales volume in 1H20 grew by 8% YoY (-3% YoY in 1Q20 / +15% YoY in 2Q20), while after-sales service volume increased by 9% YoY. The proportion of luxury brands in new car sales revenue increased to 84.3% in 1H20 from 80.0% in 1H19. Also, the proportion of luxury brands in after-sales revenue increased to 83.8% in 1H20 from 79.4% in 1H19. The expense ratio dropped by 0.57 ppt YoY in 1H20, offsetting a slight decline in GPM. As a result, the NPM increased by 0.12ppt YoY to 3.6% in 1H20. MeiDong continued to generate strong operating cash flow in 1H20 (+20.5% YoY to RMB624mn).
- Great management ability underpins its operating efficiency.** By actively facilitating orders and delivery, MeiDong's inventory turnover days dropped to 12 days (vs 23 days in 1H19). The unit revenue of incumbent stores increased by 19.9% YoY (new car sales revenue +20.7% YoY / after-sales revenue +13.5% YoY) in 1H20. The bottom-line was flat in 1Q20 (+0.4% YoY) and was resumed to its high growth path in 2Q20 (+43.2%YoY) swiftly. We believe that MeiDong will maintain its excellent operating efficiency given its strong management ability.
- Clear business objectives will foster the rapid growth of after-sales service.** Thanks to its "Single City Single Store" strategy, MeiDong has a strong customer stickiness in after-sales service by nature. In addition, MeiDong currently focuses its business objective on CRR (customer return ratio) in order to further generate revenue in the after-sales segment. The average store age of MeiDong is about four years while the median is three years. We believe that its after-sales revenue will usher in rapid growth given 1) single city single store strategy; 2) clear objective; and 3) more mature stores. The increase in the proportion of after-sales revenue will also lift its GPM and NPM further.

### Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	11,067	16,210	21,135	28,522	36,659
YoY growth (%)	44%	46%	30%	35%	29%
Net income (RMB mn)	363	551	736	1,033	1,313
EPS (RMB)	0.32	0.48	0.63	0.88	1.12
YoY growth (%)	25%	51%	32%	40%	27%
Consensus EPS(RMB)	0.28	0.47	0.61	0.84	1.10
P/E (x)	70.9	46.9	35.6	25.4	19.9
P/B (x)	18.7	15.1	12.3	9.6	7.5
Yield (%)	1%	1%	2%	2%	3%
ROE (%)	30%	36%	38%	43%	42%
Net gearing (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, Bloomberg, CMBIS estimates

**BUY (Maintain)**

Target Price **HK\$33.7**  
 (Previous TP **HK\$13.7**)  
 Up/Downside **+34.1%**  
 Current Price **HK\$25.1**

### China Auto Sector

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### Stock Data

Mkt Cap (HK\$ mn)	31,212
Avg 3 mths t/o (HK\$ mn)	102.44
52w High/Low (HK\$)	25.8/5.59
Total Issued Shares (mn)	1,244

Source: Bloomberg

### Shareholding Structure

YE Fan/HU Huanran	56.51%
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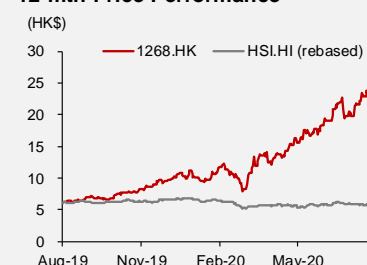
Source: HKEx

### Share Performance

	Absolute	Relative
1-mth	26.5%	27.9%
3-mth	53.1%	50.7%
6-mth	116.1%	140.6%

Source: Bloomberg

### 12-mth Price Performance



Source: Bloomberg

### Auditor: KPMG

### Related Reports

- "Meidong Auto (1268 HK) – High growth together with great efficiency" – 31 Mar 2020
- "Meidong Auto (1268 HK) – The fastest growing dealer with the best ROE" – 11 Dec 2019

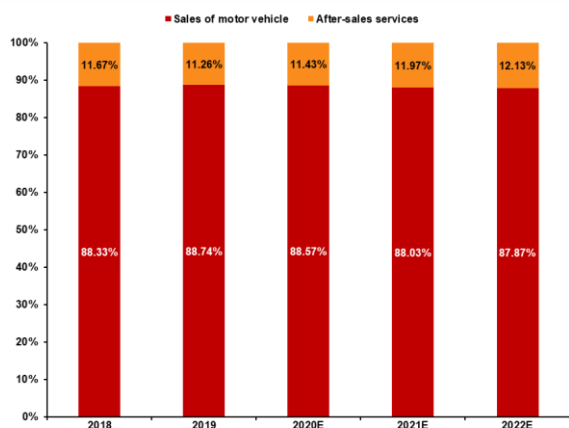
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- **Potential M&A expansion backed by strong cash on hand.** Although MeiDong only added two stores in 1H20 (+1 Lexus/+1 Porsche), we expect Meidong will newly open an additional five stores in 2H20E. In addition, the Company nearly doubled its cash balance in 1H20 (RMB 2.4bn on 30 Jun 2020 vs RMB 1.1bn on 31 Dec 2019). Meidong completed RMB1.1bn top-up placement in Jun, RMB790mn of which aiming for future M&A. If we take a single store price of RMB45mn as a key assumption, Meidong is expected to add 18 stores through M&A. We also appreciate the stringent criteria set up for M&A target selection. In order to conform to its overall business strategy, the potential target needs to have features of 1) single city single store, 2) familiar brand (Luxury brands + Toyota) and 3) reasonable payback period.
- **We slightly adjust up our bottom-line forecast by 1% in 2020E at RMB736mn to reflect its great performance in 1H20.** Along with overall market recovery, we believe MeiDong will continue to outperform in 2H20E given its operating advantage. Based on our 2020E forecast, the implied bottom-line growth rate for MeiDong will be 38%YoY in 2H20E. We also lift our 2021E forecast by 20% to reflect 1) higher after-sales revenue growth assumption and 2) higher operating efficiency.
- **MeiDong still has upside potential in terms of valuation.** The Company adheres to the “single city single store + luxury brand” strategy in the business expansion. Equipped with the excellent management team, MeiDong continues to increase its return on capital while expanding its business. We expect the Company will deliver a CAGR of 34% in NP between 2020E and 2022E. We take 34x 2021E P/E (corresponding to 1x PEG) and raise our TP to HK\$33.7 with an upside of 34.1% from initial TP HK\$13.1 (based on initial 19.5x 2020E P/E). Reiterate BUY.

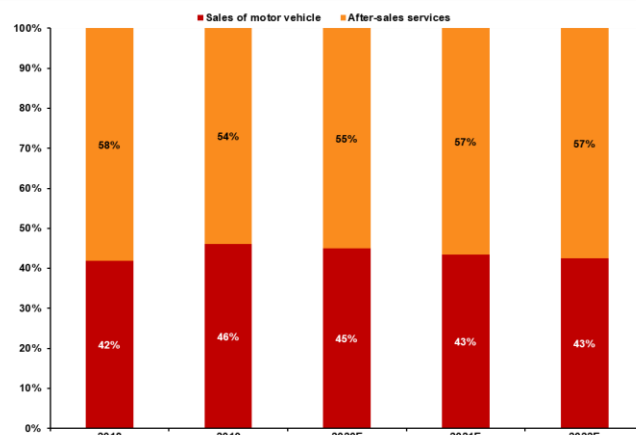
## Focus Charts

**Figure 1: Revenue composition**



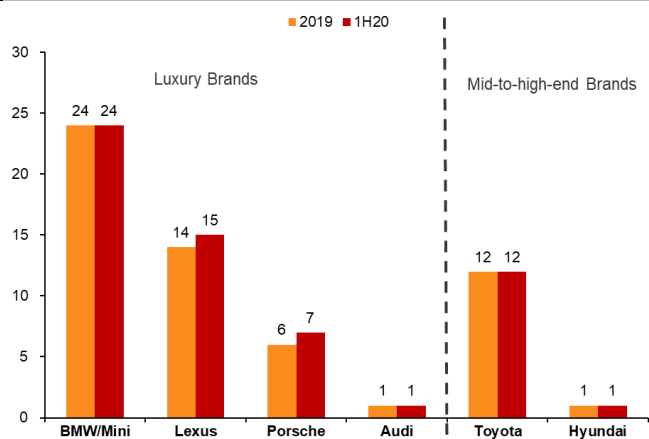
Source: Company data, CMBIS estimates

**Figure 2: GP composition**



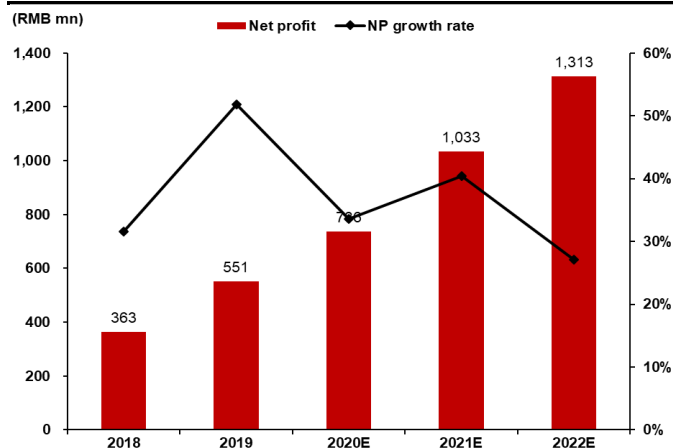
Source: Company data, CMBIS estimates

**Figure 3: Brands mix of MeiDong**



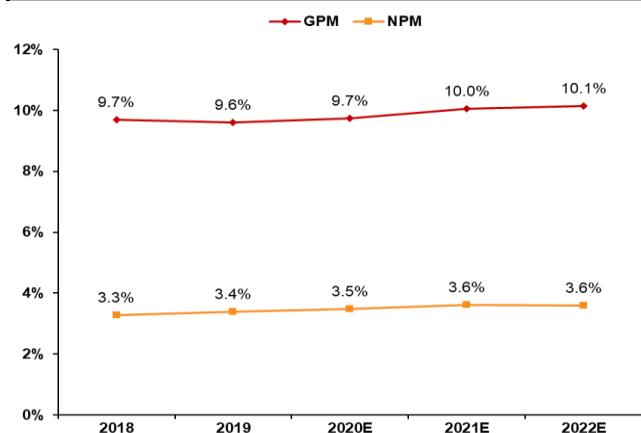
Source: Company data, CMBIS

**Figure 4: Bottom-line: high growth potential**



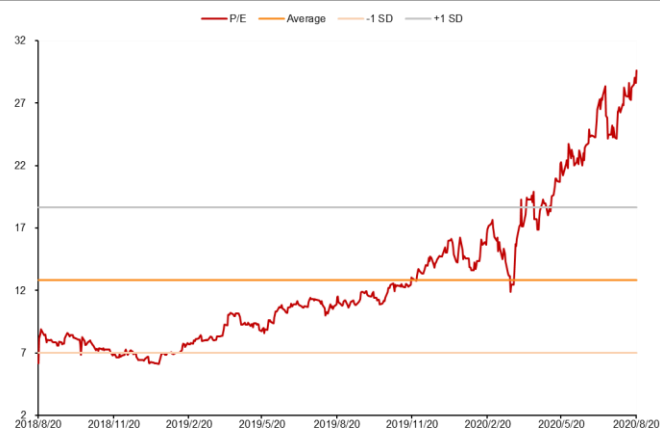
Source: Company data, CMBIS estimates

**Figure 5: Profitability is expected to improve further**



Source: Company data, CMBIS estimates

**Figure 6: PE Chart: rating will continue**



Source: Bloomberg, CMBIS

## Earnings Revision

Figure 7: Earnings revision

(RMB mn)	New		Old		Change (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Revenue	21,135	28,522	20,591	25,367	3%	12%
Gross profit	2,057	2,866	2,070	2,532	-1%	13%
Net profit	736	1,033	729	860	1%	20%
EPS (RMB)	0.63	0.88	0.63	0.74	0%	19%
Gross margin	9.73%	10.05%	10.05%	9.98%	-0.3 ppt	0.1 ppt
Net Margin	3.48%	3.62%	3.54%	3.39%	-0.1 ppt	0.2 ppt

Source: CMBIS estimates

Figure 8: CMBIS estimates vs consensus

(RMB mn)	CMBIS		Consensus		Diff (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Revenue	21,135	28,522	20,030	25,651	6%	11%
Gross profit	2,057	2,866	2,007	2,665	3%	8%
Net profit	736	1,033	721	1,014	2%	2%
EPS (RMB)	0.63	0.88	0.61	0.84	3%	5%
Gross margin	9.73%	10.05%	10.02%	10.39%	-0.3 ppt	-0.3 ppt
Net Margin	3.48%	3.62%	3.60%	3.95%	-0.1 ppt	-0.3 ppt

Source: Bloomberg, CMBIS estimates

Figure 9: Revenue breakdown

(RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Sales of motor vehicle	9,775	14,384	18,720	25,107	32,213
...YoY	44%	47%	30%	34%	28%
Luxury and ultra-luxury brands	7,437	11,693	15,752	21,802	27,856
...YoY	55%	57%	35%	38%	28%
Mid- to high-end brands	2,338	2,691	2,969	3,305	4,358
...YoY	17%	15%	10%	11%	32%
After-sales services	1,292	1,826	2,415	3,415	4,445
...YoY	43%	41%	32%	41%	30%
<b>Total</b>	<b>11,067</b>	<b>16,210</b>	<b>21,135</b>	<b>28,522</b>	<b>36,659</b>
...YoY	44%	46%	30%	35%	29%

Source: Company data, CMBIS estimates

Figure 10: P&L forecast

(RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Revenue</b>	<b>11,067</b>	<b>16,210</b>	<b>21,135</b>	<b>28,522</b>	<b>36,659</b>
...YoY	44.05%	46.47%	30.38%	34.95%	28.53%
Cost of sales	(9,994)	(14,652)	(19,078)	(25,656)	(32,944)
<b>Gross profit</b>	<b>1,073</b>	<b>1,558</b>	<b>2,057</b>	<b>2,866</b>	<b>3,715</b>
GPM (%)	9.70%	9.61%	9.73%	10.05%	10.13%
...YoY	31.02%	45.82%	31.79%	39.32%	29.61%
Selling Exp	(391)	(493)	(651)	(913)	(1,210)
...% of rev	-3.53%	-3.04%	-3.08%	-3.20%	-3.30%
Admin Exp	(313)	(382)	(507)	(699)	(898)
...% of rev	-2.83%	-2.36%	-2.40%	-2.45%	-2.45%
<b>Net profit</b>	<b>363</b>	<b>551</b>	<b>736</b>	<b>1,033</b>	<b>1,313</b>
NPM (%)	3.28%	3.40%	3.48%	3.62%	3.58%
...YoY	31.52%	51.79%	33.55%	40.37%	27.13%

Source: Company data, CMBIS estimates

## Financial Summary

### Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Revenue</b>	<b>11,067</b>	<b>16,210</b>	<b>21,135</b>	<b>28,522</b>	<b>36,659</b>
Sales of motor vehicle	9,775	14,384	18,720	25,107	32,213
After-sales services	1,292	1,826	2,415	3,415	4,445
Cost of sales	(9,994)	(14,652)	(19,078)	(25,656)	(32,944)
<b>Gross profit</b>	<b>1,073</b>	<b>1,558</b>	<b>2,057</b>	<b>2,866</b>	<b>3,715</b>
S&D expenses	(391)	(493)	(651)	(913)	(1,210)
Admin expenses	(313)	(382)	(507)	(699)	(898)
Credit/asset impairment	0	0	0	0	0
Other income	154	154	205	282	348
Other expenses	0	0	0	0	0
Finance expenses	(63)	(123)	(135)	(162)	(198)
PL from JVs	31	44	47	52	57
PL from Associates	0	0	0	0	0
<b>Profit before income tax</b>	<b>491</b>	<b>757</b>	<b>1,016</b>	<b>1,427</b>	<b>1,814</b>
Income tax expense	(128)	(200)	(268)	(376)	(478)
<b>Profit for the year</b>	<b>363</b>	<b>558</b>	<b>749</b>	<b>1,051</b>	<b>1,336</b>
<b>Less: MI</b>	<b>1</b>	<b>7</b>	<b>13</b>	<b>18</b>	<b>23</b>
<b>Net Profit</b>	<b>363</b>	<b>551</b>	<b>736</b>	<b>1,033</b>	<b>1,313</b>

### Cash flow

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Net income</b>	<b>363</b>	<b>551</b>	<b>736</b>	<b>1,033</b>	<b>1,313</b>
D&A	67	63	85	123	160
Change in working	(1,043)	(1,380)	(1,164)	(1,908)	(2,155)
Others	901	1,697	1,649	2,362	2,740
<b>Net cash from</b>	<b>288</b>	<b>931</b>	<b>1,305</b>	<b>1,611</b>	<b>2,057</b>
Capex & investments	(385)	(390)	(569)	(794)	(1,008)
Associated companies	19	-	-	-	-
Others	158	107	-	-	-
<b>Net cash from</b>	<b>(208)</b>	<b>(283)</b>	<b>(569)</b>	<b>(794)</b>	<b>(1,008)</b>
Equity raised	4	-	8	-	-
Change of Debts	356	(62)	99	261	405
Dividend paid	(149)	(145)	(303)	(442)	(568)
Others	31	(183)	-	-	-
<b>Net cash from</b>	<b>242</b>	<b>(390)</b>	<b>(196)</b>	<b>(180)</b>	<b>(163)</b>
<b>Net change in cash</b>	<b>322</b>	<b>258</b>	<b>540</b>	<b>636</b>	<b>886</b>
Cash at the beginning	811	1,284	2,086	2,626	3,262
Exchange difference	151	544	-	-	-
<b>Cash at the end</b>	<b>1,284</b>	<b>2,086</b>	<b>2,626</b>	<b>3,262</b>	<b>4,149</b>
Less: pledged cash	417	962	962	962	962

### Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Non-current assets</b>	<b>1,163</b>	<b>2,139</b>	<b>2,636</b>	<b>3,345</b>	<b>4,199</b>
Fixed asset	858	1,035	1,259	1,599	2,031
Intangible assets	69	65	151	266	407
Interest in JV/associate	44	55	63	70	77
Other non-current assets	192	984	1,163	1,411	1,684
<b>Current assets</b>	<b>3,012</b>	<b>3,786</b>	<b>4,647</b>	<b>5,995</b>	<b>7,678</b>
Cash	1,284	2,086	2,626	4,149	4,149
Account receivable	889	1,159	1,363	1,833	2,353
Inventory	839	541	658	900	1,177
Other current assets	-	-	-	-	-
<b>Current liabilities</b>	<b>2,616</b>	<b>3,180</b>	<b>3,941</b>	<b>5,107</b>	<b>6,545</b>
Borrowings	1,029	871	962	1,164	1,496
Account payables	1,550	2,132	2,765	3,665	4,706
Other payables	0	85	99	122	147
Tax payables	37	92	115	156	196
<b>Non-current liabilities</b>	<b>159</b>	<b>975</b>	<b>1,144</b>	<b>1,412</b>	<b>1,713</b>
Borrowings	144	240	248	307	381
Provisions	-	-	-	-	-
Deferred income tax	15	9	32	45	57
Others	-	726	864	1,059	1,275
<b>Shareholders' equity</b>	<b>1,379</b>	<b>1,711</b>	<b>2,127</b>	<b>2,734</b>	<b>3,509</b>
<b>Minority Interest</b>	<b>21</b>	<b>58</b>	<b>71</b>	<b>89</b>	<b>110</b>
<b>Total net assets</b>	<b>1,400</b>	<b>1,770</b>	<b>2,198</b>	<b>2,822</b>	<b>3,619</b>

### Key ratios

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Sales mix (%)</b>					
Sales of motor vehicle	88%	89%	89%	88%	88%
After-sales services	12%	11%	11%	12%	12%
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>
<b>P&amp;L ratios (%)</b>					
Gross profit margin	10%	10%	10%	10%	10%
Pre-tax margin	4%	5%	5%	5%	5%
Net margin	3%	3%	3%	4%	4%
Effective tax rate	26%	26%	26%	26%	26%
<b>Balance sheet ratios</b>					
Current ratio (x)	1.15	1.19	1.18	1.17	1.17
Quick ratio (x)	0.83	1.02	1.01	1.00	0.99
Cash ratio (x)	0.49	0.66	0.67	0.64	0.63
Inventory days	31	13	13	13	13
AP days	57	53	53	52	52
AR days	29	26	26	26	26
Total debt / total equity	84%	104%	94%	90%	87%
Net debt / equity ratio	net cash	net cash	net cash	net cash	net cash
<b>Returns (%)</b>					
ROE	30%	36%	38%	43%	42%
ROA	15%	17%	17%	19%	19%
<b>Per share</b>					
EPS (RMB)	0.32	0.48	0.63	0.88	1.12
DPS (RMB)	0.13	0.26	0.38	0.49	0.62
BVPS (RMB)	1.20	1.48	1.82	2.34	3.00

Source: Company data, CMBIS estimates

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