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CMBI Credit Commentary

Car Inc: Better than expected 1H22 results, buy CARINC'24 as a carry play

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Buy CARINC'24 as a carry play in the non-distressed HY space

Offer at 85.2 CARINC '24 is trading at a YTM of 21.9%. We recommend buy on CARINC'24 as a carry play in the non-distressed space. While a full recovery to the pre-pandemic level remains challenging given the stringent COVID-19 policy and sporadic pandemic outbreak in China, we take comfort that Car Inc. (Car) has been adjusting its fleet size efficiently. It has also opened up finance lease as a new funding channel to purchase new vehicle. Between CARINC and EHICAR, we are more comfortable with CARINC for the time being as we have more data points after Car announced the better-than-expected operating results in 1H22 when key cities in China were under strict lock-down, and car rental operations was under severe pressure. We shall provide updates on EHICAR after the interim result announcement in Sep'22.

Better than expected 1H22 results in a challenging operating environment

	1H21	1H22	2Q21	1Q22	2Q22
Average fleet	89,756	82,285	88,506	82,788	81,788
Utilization rate	62.8%	62.8%	68.7%	67.5%	58.1%
ADRR (RMB)	191	187	193	195	179
RevPAC (RMB)	120	118	133	131	104

Due mainly to the strict lock-down policy in 2Q22, Car's operating performance weakened notably. In 1H22, its revenue and EBITDA declined 8.4% and 23.7% to RMB2.3bn and RMB721.8m, respectively. The EBITDA margin narrowed to 31.3% in 1H22 from 37.5% in 1H21. That said, we take some comfort that Car has been flexible in adjusting its fleet size such that the overall utilization rate in 1H22 were largely flat, and impact on ADRR and RevPAC were contained. As per Car, operating statistics showed notable improvement in Jul'22 and early Aug'22. ADRR, RevPAC and utilization rate rebounded to RMB233, RMB160 and 68.6%, respectively. The improving trends continued up to the first half of Aug'22 but had moderated since then given the sporadic outbreak of COVID-19. We expect its operating performance to rebound from that in 2Q22 although a full recovery to the pre-pandemic level remains challenging in the near-term.

Finance lease as a new funding channel for more active fleet replenishment

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Car has been actively adding new vehicles starting 2Q22 in anticipation of more relaxed COVID-19 policies. In 2Q22, its net fleet addition is 8,353 units compared with net reductions of 3,236 units in 1Q22 and 3,764 units in 4Q22. The net fleet investments in 1H22 was RMB1.5bn. Given the slow progress in securing new bank loans, Car turned to finance leases for new vehicle acquisitions. Car obtained new facilities of RMB2.7bn in 1H22 (RMB8bn YTD), most of them are finance leases and cRMB3bn remains undrawn as at Jun'22. Car plans to acquire new vehicles of 30-40k units in 2H22 for RMB3-4bn. It plans to sell used vehicles of 20-30k units for RMB900mn-1.3bn over 2H22. As per our discussions with Car, the funding cost of finance leases is 7-8% while that of bank loans is 5-6%. In general, the down-payments for using bank loans to acquire vehicles is 20-30%. We estimate the down-payments for using finance leases is c40% based on deposit of RMB500mn paid in 1H22. Finance lease offer an alternative funding channel for Car to adjust its fleet size in view of increasing demand, although the funding cost and down-payment requirements are higher.

Weakened coverage ratio but liquidity profile remains adequate

Given the weakened 1H22 results, its credit profile deteriorated with net debt/EBITDA and EBITDA/int ratios at 3.6x and 2.8x in 1H22 compared with 2.1x and 3.3x in 1H21, respectively. However, we take comfort with Car's ability to consistently generate positive free cash flow, partly through fleet size adjustment and sales of used vehicles. In 1H22, its free cash flow was RMB692mn. Even in 2Q22 when the operating environment was considerably affected by the strict lock-down policy, Car generated positive free cash flow of cRMB158mn. Car guided that its cash inflow from car rental operations and sales of used vehicle would be RMB2-2.4bn while the down-payment for acquisitions of new vehicles to cRMB1bn In 2H22. Its cash balance as at the FYE22 would be cRMB1bn, roughly the same as that in Jun'22. Subsequent to the full repayment of USD bonds of 372.3mn in 1H22, the only offshore bonds (except the CBs of USD175mn placed to its shareholder MBK, puttable in Jan'24) of Car is CARINC'24 (o/s USDS250mn due Mar'24). We believe that its offshore maturities are manageable.

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