

China Meidong Auto (1268 HK)

The terrible 2023 is behind us

Maintain BUY. We estimate that Meidong's net profit excluding impairment and withholding tax impact in 2H23E could be a similar level to that in 1H23, as the higher portion of after-sales service profit and cost cuts could offset the HoH decline for new-car GPM. However, we are of the view that impairment for goodwill and/or intangible assets is likely in 2H23E. We project FY24E net profit to be RMB371mn, as Porsche's new-car GPM is likely to improve from 2Q24E. We expect BMW and Lexus to continue facing headwinds in FY24E, which could force Meidong to adopt a more conservative approach in new-car sales.

■ **2H23 earnings under pressure on lower new-car margins and goodwill impairment risk.** We project Meidong's new-car sales volume to rise 1% HoH in 2H23E to about 32,000 units (Porsche: ~5,200 units, BMW: ~11,700 units). However, we expect new-car revenue to fall 8% HoH due to lower average selling prices (ASP), as we estimate the ASP for Porsche to fall by RMB13,000 HoH and BMW to decline by RMB7,500 HoH. We expect after-sales service revenue to rise 11% YoY and 5% HoH to RMB2.1bn.

We project Meidong's new-car GPM to turn negative (-0.4%) in 2H23E, as we expect new-car GPM to remain the same HoH for Porsche and drop by 1ppt HoH for BMW and rise by 0.4ppt for Lexus. Accordingly, we expect Meidong's overall GPM to widen 0.4ppt HoH to 7.5% in 2H23E due to the larger contribution from after-sales services.

We see the possibility for goodwill and intangible assets impairment in 2H23, but it is quite difficult for us to quantify. We assume an impairment loss of RMB100mn in 2H23E, which will also result in a higher effective tax rate, as impairment is not deductible for taxes. We estimate Meidong's net profit to be RMB41mn under such assumptions. It would imply that net profit excluding impairment in 2H23E would be about RMB65mn higher than that in 1H23.

■ **Porsche has the highest chance of posting a better new-car GPM in FY24 among all the brands.** Based on our channel checks, Porsche's sales targets for Jan and Feb 2024 are quite low in a bid to cut inventories. We expect its new-car GPM to improve from 2Q24 amid a reasonable inventory level and the launch of the new *Panamera*. We project Porsche's retail sales volume to drop 13% YoY to about 70,000 units in China in 2024 and Meidong to account for 15% of it. We also project Porsche's new-car GPM at Meidong to widen by 0.5ppt YoY to 2.5% in FY24E. That would increase Meidong's new-car gross profit by about RMB24mn YoY in FY24E.

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	23,577	28,655	27,343	25,494	26,657
YoY growth (%)	36.1	(9.1)	(20.8)	10.1	15.9
Net income (RMB mn)	1,166	521	80	371	697
EPS (RMB)	0.92	0.41	0.06	0.27	0.52
YoY growth (%)	55.3	(55.3)	(84.6)	363.9	87.8
P/E (x)	2.5	6.2	43.4	9.4	5.0
P/B (x)	0.7	0.8	0.7	0.6	0.6
Yield (%)	2.6	1.0	0.8	5.3	10.0
ROE (%)	32.5	12.7	1.7	7.0	12.2
Net gearing (%)	Net cash	21	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	HK\$ 4.00
(Previous TP	HK\$ 7.20)
Up/Downside	+40.4%
Current Price	HK\$ 2.85

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Stock Data

Mkt Cap (HK\$ mn)	3,837
Avg 3 mths t/o (HK\$ mn)	33
52w High/Low (HK\$)	21.50/2.82
Total Issued Shares (mn)	1,346
Source: Bloomberg	

Shareholding Structure

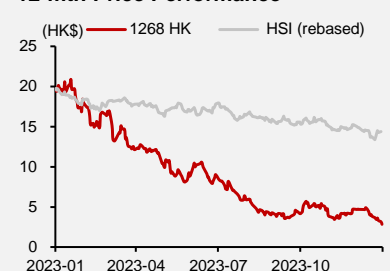
Apex Sail Limited	52.2%
Others	47.8%
Source: HKEx	

Share Performance

	Absolute	Relative
1-mth	-40.0%	-32.1%
3-mth	-33.9%	-25.7%
6-mth	-65.3%	-46.2%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: KPMG

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- **BMW and Lexus still face challenges in FY24E.** Based on our estimates, BMW's new-car gross profit fell by RMB3,500 per vehicle HoH in 2H23E, despite HoH subsidy increase of RMB4,000 per vehicle. The new-car margin deterioration has been continuing in 1Q24, based on our channel checks. BMW targets 6% YoY growth for retail sales volume in China, which is too aggressive in our view, despite its new-generation 5 Series launched in Jan 2024. The new Mercedes-Benz *E Class*, which was rolled out about one month ago, has already started to provide discounts, based on our channel checks. BMW also targets 20% of its China retail sales volume to be NEVs in 2024, which could also lower its dealers' margins, given the *i5*'s less competitive pricing than its peers, in our view.

We are of the view that new-car GPM for Lexus' dealers in 2024 could largely depend on subsidies, which makes our forecasting more difficult. Lexus targets retail sales volume of 0.18mn units in China in 2024, or flat YoY. We project BMW's and Lexus' new-car GPM to be -2% and -1.5% in FY24E, respectively.

- **We expect Meidong to adopt a conservative approach in new-car sales and cut costs aggressively.** We do not expect new store openings for FY24E and we cannot rule out a possibility to close more stores after closing two in FY23E. We are of the view that Meidong still takes a cautious approach and is selective in partnering with NEV start-ups. We project Meidong's new-car sales volume and revenue to drop 8% YoY and 9% YoY in FY24E, respectively, as negative new-car GPM could force dealers to sell fewer cars in order to cut loss.

We project after-sales service revenue to rise 9% YoY in FY24E, which would make after-sales services account for 17% of Meidong's total revenue in FY24E. That would lift its overall GPM to 8.6% in FY24E on our estimates, despite limited improvement from new-car GPM.

We estimate SG&A ratio to drop from 6.3% in FY23E to 6.1% in FY24E, despite continuous amortization from intangible assets, as Meidong has been quite aggressive in cost reduction. We assume no impairment loss in FY24E, as the situation for Porsche is likely to improve. We still expect a high effective tax rate amid the withholding tax from the internal dividends to offshore subsidiaries in order to make the repayment ready for the convertible bond redemption in Jan 2025. Such redemption would reduce finance costs significantly in FY25E, which is likely to result in YoY growth for net profit in FY25E, although the visibility is still very low now.

- **Valuation/Key risks.** Accordingly, we project FY24E net profit to be RMB371mn, or 50% lower than our prior forecast. We maintain our BUY rating but cut our target price from HK\$7.20 to HK\$4.00, which is still based on 13x our revised FY24E EPS, as the valuation premium for its management could narrow during tough times. Key risks to our rating and target price include lower sales and/or margins than our expectation, as well as a sector de-rating.

Figure 1: 2H23E earnings preview

RMB mn	1H21	2H21	1H22	2H22	1H23	2H23E	YoY	HoH
New-car sales volume (units)	32,221	29,374	29,658	38,213	31,589	31,929	-16.4%	1.1%
Total revenue	11,808	11,769	12,658	15,996	14,089	13,254	-17.1%	-5.9%
Gross profit	1,274	1,497	1,334	1,183	1,001	993	-16.1%	-0.8%
Selling exp.	(348)	(393)	(398)	(462)	(382)	(391)	-15.4%	2.3%
Admin exp.	(278)	(301)	(377)	(433)	(438)	(515)	18.9%	17.7%
Operating profit	771	927	668	446	305	238	-46.5%	-21.8%
Net profit	537	629	343	178	39	41	-76.9%	5.2%
Gross margin	10.8%	12.7%	10.5%	7.4%	7.1%	7.5%	0.1 ppt	0.4 ppt
Operating margin	6.5%	7.9%	5.3%	2.8%	2.2%	1.8%	-1.0 ppt	-0.4 ppt
Net margin	4.5%	5.3%	2.7%	1.1%	0.3%	0.3%	-0.8 ppt	0.0 ppt

Source: Company data, CMBIGM estimates

Figure 2: Earnings revision

(RMB mn)	New			Old			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	27,343	25,494	26,657	28,859	28,934	30,704	-5.3%	-11.9%	-13.2%
Gross profit	1,994	2,196	2,546	2,281	2,713	3,039	-12.6%	-19.0%	-16.2%
Operating profit	543	902	1,218	888	1,460	1,697	-38.9%	-38.2%	-28.2%
Net profit	80	371	697	339	749	974	-76.4%	-50.4%	-28.5%
Gross margin	7.3%	8.6%	9.6%	7.9%	9.4%	9.9%	-0.6 ppt	-0.8 ppt	-0.3 ppt
Operating margin	2.0%	3.5%	4.6%	3.1%	5.0%	5.5%	-1.1 ppt	-1.5 ppt	-1.0 ppt
Net margin	0.3%	1.5%	2.6%	1.2%	2.6%	3.2%	-0.9 ppt	-1.1 ppt	-0.6 ppt

Source: CMBIGM estimates

Figure 3: CMBI estimates vs consensus

(RMB mn)	CMBIGM			Consensus			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	27,343	25,494	26,657	29,201	30,668	33,119	-6.4%	-16.9%	-19.5%
Gross profit	1,994	2,196	2,546	2,233	2,800	3,263	-10.7%	-21.6%	-22.0%
Operating profit	543	902	1,218	764	1,296	1,664	-28.9%	-30.4%	-26.8%
Net profit	80	371	697	267	687	870	-70.1%	-46.0%	-19.9%
Gross margin	7.3%	8.6%	9.6%	7.6%	9.1%	9.9%	-0.4 ppt	-0.5 ppt	-0.3 ppt
Operating margin	2.0%	3.5%	4.6%	2.6%	4.2%	5.0%	-0.6 ppt	-0.7 ppt	-0.5 ppt
Net margin	0.3%	1.5%	2.6%	0.9%	2.2%	2.6%	-0.6 ppt	-0.8 ppt	0.0 ppt

Source: Bloomberg, CMBIGM estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue	23,577	28,655	27,343	25,494	26,657
Cost of sales	(20,806)	(26,137)	(25,348)	(23,297)	(24,111)
Gross profit	2,771	2,517	1,994	2,196	2,546
Other income	247	267	274	269	277
Distribution expenses	(741)	(860)	(773)	(756)	(779)
Administrative expenses	(578)	(811)	(953)	(807)	(826)
Operating profit	1,698	1,114	543	902	1,218
Finance costs	(133)	(275)	(288)	(250)	(151)
Share of profits of assos	-	-	-	-	-
Share of profits of JVs	48	25	18	13	12
Profit before tax	1,613	864	273	665	1,079
Taxation	(399)	(308)	(183)	(239)	(287)
Minority interests	(48)	(35)	(10)	(55)	(95)
Net profit	1,166	521	80	371	697

Cash flow summary

YE 31 Dec (RMB mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Profit before taxation	1,613	864	273	665	1,079
Depreciation/amortization	287	490	568	568	593
Change in working capital	276	67	(175)	76	694
Others	(364)	(267)	130	(107)	(246)
Net cash from operating	1,812	1,154	797	1,202	2,120
Capex	(363)	(283)	(120)	(140)	(220)
Others	(1,019)	(3,200)	197	26	(114)
Net cash from investing	(1,382)	(3,483)	77	(114)	(334)
Share issuance	11	647	934	10	10
Dividend paid	(475)	(1,027)	(184)	(120)	(306)
Others	146	1,708	(1,201)	(379)	(2,527)
Net cash from financing	(317)	1,328	(451)	(489)	(2,823)
Net change in cash	112	(1,002)	423	598	(1,038)
Cash at beginning of the year	2,538	2,622	1,636	2,059	2,657
Exchange difference	(29)	16	-	-	-
Cash at the end of the year	2,622	1,636	2,059	2,657	1,619

Balance sheet

YE 31 Dec (RMB mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Current assets	5,563	5,888	6,409	6,735	5,099
Cash and equivalents	2,622	1,636	2,059	2,657	1,619
Accounts receivables	1,817	1,560	1,648	1,676	1,753
Inventories	355	1,069	903	702	727
Other current assets	769	1,623	1,800	1,700	1,000
Non-current assets	4,240	8,351	7,713	7,455	7,603
PP&E	1,381	1,843	1,672	1,573	1,577
Intangibles	546	3,477	3,291	3,207	3,215
Interests in JVs and assos	62	39	37	37	38
Other non-current assets	2,250	2,992	2,713	2,638	2,773
Total assets	9,803	14,239	14,123	14,191	12,702
Current liabilities	4,089	4,874	3,977	3,685	3,807
Short-term debt	989	1,414	600	500	500
Accounts payable	2,788	3,193	3,125	2,936	3,039
Other current liabilities	312	267	252	249	268
Non-current liabilities	1,597	4,932	4,817	4,842	2,715
Long-term debt	299	2,768	2,730	2,780	493
Other non-current liabilities	1,297	2,164	2,087	2,062	2,222
Total liabilities	5,686	9,806	8,794	8,526	6,522
Share capital	100	102	109	109	109
Reserves	3,847	4,173	5,058	5,377	5,864
Minority interests	170	159	162	178	207
Shareholders' equity	3,947	4,275	5,167	5,486	5,973
Total equity and liabilities	9,803	14,239	14,123	14,191	12,702

Key ratios

YE 31 Dec	FY21A	FY22A	FY23E	FY24E	FY25E
Sales mix (%)					
Sales of new vehicles	88.3	88.3	85.3	82.8	83.1
After-sales services	11.7	11.7	14.7	17.2	16.9
Growth (%)					
Revenue	16.7	21.5	(4.6)	(6.8)	4.6
Gross profit	36.1	(9.1)	(20.8)	10.1	15.9
Operating profit	48.2	(34.4)	(51.3)	66.2	35.0
Net profit	55.3	(55.3)	(84.6)	363.9	87.8
Profit & loss ratio (%)					
Gross margin	11.8	8.8	7.3	8.6	9.6
Operating margin	7.2	3.9	2.0	3.5	4.6
Net profit margin	4.9	1.8	0.3	1.5	2.6
Balance sheet ratio					
Net cash/total equity (x)	0.5	(0.2)	0.1	0.2	0.3
Current ratio (x)	1.4	1.2	1.6	1.8	1.3
Receivable turnover days	28.1	19.9	22.0	24.0	24.0
Inventory turnover days	6.2	14.9	13.0	11.0	11.0
Payable turnover days	48.9	44.6	45.0	46.0	46.0
Profitability (%)					
ROE	32.5	12.7	1.7	7.0	12.2
ROA	13.3	4.3	0.6	2.6	5.2
Per share data (RMB)					
EPS	0.92	0.41	0.06	0.27	0.52
DPS	0.83	0.20	0.03	0.14	0.26

Source: Company data, CMBIGM estimates

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