

13 March, 2017

Yadea (1585.HK)

As a leader in electric two-wheeled vehicles, Yadea delivered stable sales and YoY earnings growth in FY16. The slowdown in 1H16 YoY growth for low-end electric scooters has led management to switch to differential price discounts on its products which it could maintain gross margin. Market strategy and high-end positionings for several years have borne fruit for Yadea with a likely rapid sales growth in 2M17. We see sales momentum pickups from FY17 onwards. Coupled with sales momentum recovery, clean balance sheet and attractive valuation, we reiterate Buy.

Investment Highlights

- ▶ **Yadea delivered stable sales and earnings growth of 3.6% and 14.6% in FY16.** Such growth was driven by introducing 92 new electric two-wheeled vehicles and gross margin expansion to 20.3% in FY16 from 18.9% in FY15.
- ▶ **The slowdown in 2H16 sales volume YoY growth has led the management to switch marketing strategy to offer differential price discounts in 2M17, which likely successfully boost sales growth and maintain gross margin over FY17E- FY18E.** After several years of high-end brand buildings where widely recognized by public, its marketing strategy has borne fruit. Offering price discounts on mid-long end products may lead to rapid sales growth while charging higher price on superior quality of electric scooters with lithium battery is able to past the cost to customers.
- ▶ **Strong bargaining power over suppliers, stable sales and IPO has led to abundant cash.** Payable turnover days increased from 174 days in FY15 to 212 days in FY16. Yadea processed net cash of RMB 1.8 billion, representing market cap of 35%.
- ▶ **We see sales momentum pickups over FY17 onwards and stable gross margin should bode well for the share price.** We reiterate Buy with its clean balance and attractive valuation of FY16 PE and PB of 9.4x and 1.8x.

Flash Note

13 March, 2017

Buy

Last price :

HK\$1.71

Stock Data

Number of shares outstanding: 3,000 million

Mkt cap: HK\$5,130 million

Financial Summary

Year-End (Source: Company, BMIF Estimates)	FY13	FY14	FY15	FY16
Sales (RMB: Million)	5,059	5,824	6,429	6,662
Growth	-	15%	10%	4%
Net Profit (RMB: Million)	174	223	375	430
Growth	-	28%	68%	15%
Basic EPS (RMB)	-	-	0.18	0.16
Growth	-	-	-	-9.9%
PE(x)	-	-	-	9.4
PB(x)	-	-	-	1.8

Stable FY16 Result

Yadea delivered stable FY16 sales and net profit growth of 3.6%YoY and 14.6%YoY to RMB 6.6 billion and RMB 430 million, with gross margin expansion to 20.3% in FY16 from 18.9% in FY15. Excluding IPO expense, Equity-settled share award expense and gains from financial asset, adjusted earnings grew by 6.2%yoy to RMB 415 million. Such improvement was driven by introducing 92 new electric two-wheeled vehicles and upgraded the existing models, which allowed to charge higher selling price. Average selling price (ASP) has slight increases, with electric scooters and electric bicycles' ASP of RMB1,766 and RMB1,181 in FY16, compared to RMB 1,704 and RMB 1,140 in FY15.

The slowdown in 2H16 sales volume YoY growth has led the management to switch marketing strategy to offer price differential discounts in 2M17, which likely successfully boost sales growth and maintain gross margin over FY17E- FY18E. 2H16 sales grew by 1.6%yoy (+26.8%qoq) while 2H16 sales volume dropped by 2.5%yoy (+29.1%qoq) where the second half year usually is a peak season. The slowdown in 2H16 YoY sales volume was dragged down by electric scooters of a negative YoY growth of 4.3% (+26.2%qoq), especially low-end scooters. Management indicted to switch pricing strategy in 2M17 to offer price discount discounts by enhancing product mix, where it offered price discounts to mid-low end products and charged higher price to high-end products. Management suggested sales YoY growth of 30% in 2M17. We expect that sales momentum pickups and stable gross margin should bode well for the share price.

With strong bargaining power over suppliers, payable turnover days increased from 174 days in FY15 to 212 days in FY16. As a top player of China two-wheeled electric vehicles with 10.5% of market share in FY15, Yadea had strong bargaining power over suppliers. FY16 trade and bills payable gained by 34%yoy and 5%yoy to RMB1.2 billion and RMB 2billion in FY16, representing payable turnover days up from 174 days in FY15 to 212 days in FY16.

Prudent and strong cash flow management and healthy balance sheet in FY16. Yadea had strong cash flow. On the back of IPO in FY15, stable sales and strong bargaining power over suppliers and distributors, cash increased by 129%yoy to RMB 1.8 billion in FY16 without any borrowings, representing 35% of its market cap. However, interest income dipped by 30%yoy to RMB 13 million due to the interest rate cut in China savings deposits. Management mentioned to consider potential diversified financial investments.

Sales And Marketing Strategy In FY17

After widely recognized by customers and building premium brands, sales jumped in the first two months in FY17 by enhancing product mix and price discounts. As several years of market strategy and high end position have borne fruit for Yadea, management suggested Yadea to have a rapid YoY sale of 30% in 2M17 by price discounts in Chinese New Year, which used to be a low season. Yadea earned much huger growth by offering discount on its products, compared to low-end competitors which also offered discounts to their products. Management has very positive sales outlook in FY17 on rapid sales growth, flat ASP and stable gross margin.

Management targeted to increase market share from 10.5% in FY15 to 30% in FY21 by promoting high-end products and strengthening technology know-how. The market share of the competitors has been taken by Yadea.

Yadea cooperated with Lightning Motor in developing lithium battery and management mentioned several international manufacturers plan to cooperate with Yadea. Lithium battery, which usually has been used for Yadea's high-end electric scooters, only currently accounted for 5% of total sales volumes, according to management. Lithium battery is easlier charged, higher energy ratio and longer utilization life, compared to lead-acid battery. Although lithium battery is much expensive than lead-acid battery, Yadea is able to pass the higher cost to its customers on premium-quality products. As developing lithium battery is an industry trend and immatured in China, Yadea cooperated with Lightning Motors, an U.S company specialized in R&D of advanced electric two-wheeled vehicles.

We reiterate Buy with positive outlook on stable gross margin and rapid sales growth from FY17 onwards by promoting high-end products and enhancing product mixes as Yadea has borne fruit for several years of high-end brand building. Valuation seems attractive with FY16 PE and PB of 9.4x and 1.8x, compared to peers.

Operating Ratio

Key Ratio	FY13	FY14	FY15	FY16
Gross Margin	12.9%	16.6%	18.9%	20.3%
Operating Margin	4.2%	5.2%	7.6%	8.3%
Profit Margin	3.4%	3.8%	5.8%	6.5%
Inventory Turnover Days	31.4	19.6	10.5	11.9
Receivables Turnover Days	4.7	5.2	8.4	12.7
Trade/Bills Payables Turnover Days	111.7	139.9	174.6	212
Cash Conversion Days	-75.6	-115.1	-155.7	-187.4
Return on Equity	32.2%	39.1%	57.8%	28.7%
Return on Assets	8.0%	8.1%	10.9%	8.7%
Interest Coverage	529.0	1,222.9	20,453.8	2,567.7
Current Ratio	0.87	0.87	0.93	1.30
Gearing Ratio	1.6%	0.0%	1.7%	0.0%
*Gearing ratio=Borrowings/Equity				

Source: Company

Sales Data: RMB (Excluding batteries and charges)	2013	2014	2015	2016
Sales Volume of electric two-wheeled vehicles	2,731,843	3,010,936	3,321,058	3,319,600
Sales Volume of electric scooters	1,594,618	1,869,290	2,044,610	2,029,100
Sales Volume of electric bicycles	1,137,225	1,141,646	1,276,448	1,290,500
ASP of electric two-wheeled vehicles (excluding batteries and charges)	1,852	1,934	1,936	2,007
Electric scooters	1,635	1,736	1,704	1,766
Electric bicycles	1,102	1,231	1,140	1,181

Source: Company

Peer Comparison

Valuation for Yadea is much attractive than its peers. In terms of PE, PB and ROE, valuation for Yadea is FY16 PE and PB is 9.8x and 1.8x, much attractive than automotive manufacturers industry. Yadea is expected to experience sales pickups on differential price discounts in 2M17. We reiterate Buy with its superior brand building.

	Name	Price	Market cap (HK\$m)	PE FY16E	PB FY16E	ROE FY16E
Automotive Manufacturers						
175 HK Equity	GEELY AUTOMOBILE HOLDINGS LT	11.86	105,428	20.4	4.4	13.9
1114 HK Equity	BRILLIANCE CHINA AUTOMOTIVE	13.02	65,619	16.0	2.6	16.6
1211 HK Equity	BYD CO LTD-H	44.55	142,189	20.9	2.3	12.2
1958 HK Equity	BAIC MOTOR CORP LTD-H	8.41	63,877	9.8	1.6	10.1
2238 HK Equity	GUANGZHOU AUTOMOBILE GROUP-H	13.16	155,456	10.9	1.8	18.2
2333 HK Equity	GREAT WALL MOTOR COMPANY-H	9.29	63,877	9.8	1.7	23.4
Average				14.7	2.4	15.8
Battery Manufacturers						
819 HK Equity	TIANNENG POWER INTL LTD	7.13	8,032	8.4	2.1	23.0
951 HK Equity	CHAOWEI POWER HOLDINGS LTD	6.45	7,146	8.9	2.1	19.4
Average				8.6	2.1	21.2
Electric Two Wheeled Vehicles Manufacturers						
1585 HK Equity	YADEA GROUP HOLDINGS LTD	1.7	5,100	9.8	1.8	28.7
Average				9.8	1.8	20.4

Source: Bloomberg, BMIF Estimates

Financial Summary

Income Statement

RMB ('000)	2013	2014	2015	2016	2013 Margin	2014 Margin	2015 Margin	2016 Margin	2014YoY	2015YoY	2016YoY
Sales	5,059,200	5,824,142	6,429,187	6,662,139	100%	100%	100%	100%	15%	10%	4%
Electric scooters	2,607,007	3,244,385	3,483,214	3,584,084	52%	56%	54%	54%	24%	7%	3%
Electric bicycles	1,253,472	1,405,911	1,455,416	1,523,745	25%	24%	23%	23%	12%	4%	5%
Specialty vehicles	75,331	18,429	0	0	1%	0%	0%	0%	-76%	-100%	0%
Batteries and charges	1,027,624	1,109,598	1,427,914	1,498,248	20%	19%	22%	22%	8%	29%	5%
Electric two-wheeled vehicle parts	95,766	45,819	62,643	56,062	2%	1%	1%	1%	-52%	37%	-11%
COGS	-4,404,654	-4,855,684	-5,211,994	-5,309,375	-87%	-83%	-81%	-80%	10%	7%	2%
Electric scooters	-2,147,128	-2,554,835	-2,606,385	-2,678,584	-82%	-79%	-75%	-75%	19%	2%	3%
Electric bicycles	-1,101,270	-1,166,256	-1,191,087	-1,243,145	-88%	-83%	-82%	-82%	6%	2%	4%
Gross profit	654,546	968,458	1,217,193	1,352,764	13%	17%	19%	20%	48%	26%	11%
Electric scooters	459,879	689,550	876,829	905,500	18%	21%	25%	25%	50%	27%	3%
Electric bicycles	152,202	239,655	264,329	280,600	12%	17%	18%	18%	57%	10%	6%
Other income and gains	27,184	81,280	85,770	81,027	1%	1%	1%	1%	199%	6%	-6%
Bank interest income	7,031	16,820	19,180	13,414	0%	0%	0%	0%	139%	14%	-30%
Government grants	6,372	26,478	14,138	23,594	0%	0%	0%	0%	316%	-47%	67%
Dividend income from available-for-sale investments	4,344	4,400	0	0	0%	0%	0%	0%	1%	-100%	0%
Gains from financial assets at fair value through profit or loss	10,704	23,177	42,651	37,161	0%	0%	1%	1%	117%	84%	-13%
Gain on disposal of available-for-sale investments	0	3,738	0	854	0%	0%	0%	0%	0%	100%	0%
Net gain/(loss) on disposal of PPE	-2,339	-198	988	0	0%	0%	0%	0%	-92%	-599%	-100%

	Others	1,072,	6,865	8,813	6,004	0%	0%	0%	0%	540%	28%	-32%
Selling and distribution expenses		-275,792	-349,390	-453,544	-451,191	-5%	-6%	-7%	-7%	27%	30%	-1%
Administrative expenses		-192,234	-394,616	-358,528	-427,968	-4%	-7%	-6%	-6%	105%	-9%	19%
Operating profit		213,704	305,732	490,891	554,632	4%	5%	8%	8%	43%	61%	13%
Finance cost		-427	-251	-24,000	-216	0%	0%	0%	0%	-41%	-90%	800%
Shares of JV		12,178	1,222	0	0	0%	0%	0%	0%	-90%	-100%	0%
PBT		225,455	306,703	490,867	554,416	4%	5%	8%	8%	36%	60%	13%
Tax income expense		-51,382	-83,239	-115,400	-124,287	-2%	-1%	-2%	-2%	62%	39%	8%
Profit		174,073	223,464	375,467	430,129	3%	4%	6%	6%	28%	68%	15%
Profit to equity owners		174,073	223,464	375,467	430,129	3.4%	3.8%	5.8%	6%	28%	68%	15%

Source: Company

Balance Sheet

RMB	2013	2014	2015	2016
Property, plant and equipment	447,447,000	584,301,000	679,709,000	732,980,000
Prepaid land lease payments	184,709,000	225,845,000	220,612,000	292,839,000
Intangible assets	11,262,000	12,408,000	14,162,000	16,966,000
Investment in an associate	139,081,000	0	0	0
Available-for-sale investments	75,800,000	0	8,223,000	14,683,000
Prepayments	4,008,000	3,041,000	84,600,000	59,413,000
Deferred tax assets	13,963,000	13,768,000	18,202,000	19,106,000
Total non-current assets	876,270,000	839,363,000	1,025,508,000	1,135,987,000
Inventories	361,163,000	159,621,000	141,491,000	205,000,000
Net trade and bills receivables	55,571,000	111,924,000	183,225,000	279,691,000
Trade receivables	40,667,000	105,749,000	181,799,000	280,667,000
Net trade receivable impairment	-4,090,000	-2,949,000	-1,952,000	-2,306,000
Bills receivables	18,994,000	9,124,000	3,378,000	1,330,000
Prepayments, deposits and other receivables	119,529,000	90,680,000	212,097,000	255,176,000
Due from related parties	40,000,000	0	0	
Financial assets at fair value through profit or loss	345,600,000	555,000,000	861,700,000	1,411,630,000
Pledged bank deposits	504,384,000	659,401,000	779,056,000	777,073,000
Cash and cash equivalents	283,087,000	501,322,000	786,691,000	1,801,405,000
	787,471,000	1,160,723,000	1,565,747,000	
Total current assets	1,709,334,000	2,077,948,000	2,964,260,000	4,729,975,000
Trade and bills payables	1,614,800,000	2,106,220,000	2,880,431,000	3,287,399,000
Trade payables	701,951,000	794,727,000	940,537,000	1,259,443,000
Bills payables	912,849,000	1,311,493,000	1,939,894,000	2,027,956,000
Other payables and accruals	190,215,000	265,448,000	256,740,000	285,242,000
Interest-bearing bank borrowings	10,000,000	0	12,997,000	

Due to a related party	49,000,000	0	0	
Due to the Controlling Shareholders	73,474,000	0	0	
Tax payable	20,866,000	29,070,000	35,603,000	72,751,000
Total current liabilities	1,958,355,000	2,400,738,000	3,185,771,000	3,645,392,000
Other payables			22,160,000	
Total non current liabilities			22,160,000	
Total liabilities	1,958,355,000	2,400,738,000	3,207,931,000	3,645,392,000
Share capital		135,000	135,000	188,000
Reserves	627,249,000	516,438,000	781,702,000	2,220,382,000
Total equity	627,249,000	516,573,000	781,837,000	2,220,570,000

Source: Company

Income Statement

RMB	1H15A	2H15A	1H16A	2H16A
Sales	2,752,890,000	3,676,297,000	2,937,686,000	3,724,453,000
Electric scooters	1,471,148,000	2,012,066,000	1,604,763,000	1,979,321,000
Electric bicycles	625,967,000	829,449,000	664,080,000	859,665,000
Batteries and charges	623,852,000	804,062,000	630,855,000	867,393,000
Electric two-wheeled vehicle parts	31,923,000	30,720,000	37,988,000	18,074,000
COGS	-2,241,735,000	-2,970,259,000	-2,307,494,000	-3,001,881,000
Electric scooters	-1,104,832,148	-1,501,552,852	-1,185,919,857	-1,492,664,143
Electric bicycles	-508,285,204	-682,801,796	-536,576,640	-706,568,360
Gross profit	511,155,000	706,038,000	630,192,000	722,572,000
Electric scooters	366,315,852	510,513,148	418,843,143	486,656,857
Electric bicycles	117,681,796	146,647,204	127,503,360	153,096,640
Other income and gains	30,287,000	55,483,000	38,305,000	42,722,000
Bank interest income	9,972,000	9,208,000	7,058,000	6,356,000
Government grants	2,583,000	11,555,000	12,344,000	11,250,000
Gains from financial assets at fair value through profit or loss	14,079,000	28,572,000	16,415,000	20,746,000
Gain on disposal of available-for-sale investments	1,294,000	-1,294,000	0	0
Net gain/(loss) on disposal of PPE	289,000	699,000	885,000	-31,000
Others	2,070,000	6,743,000	1,603,000	4,401,000
Selling and distribution expenses	-213,454,000	-240,090,000	-238,437,000	-212,754,000
Administrative expenses	-141,332,000	-217,196,000	-201,570,000	-226,398,000
Operating profit	186,656,000	304,235,000	228,490,000	326,142,000
Finance cost	0	-24,000	-134,000	-82,000
PBT	186,656,000	304,211,000	228,356,000	326,060,000
Tax income expense	-42,812,000	-72,588,000	-50,855,000	-73,432,000
Profit	143,844,000	231,623,000	177,501,000	252,628,000
Profit to equity owners	143,844,000	231,623,000	177,501,000	252,628,000

Source: Company

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Investment Rating System

Stock Rating (12 months)	Remark
Buy	Stocks with potential positive return exceeding 15% over the next 12 months
Hold	Stocks with potential return of between -15% to +15% over the next 12 months
Sell	Stocks with potential negative return exceeding -15% over the next 12 months
Speculative Buy	Stocks with potential positive return exceeding 20% over the next 6 months, with high volatility
Speculative Sell	Stocks with potential negative return exceeding -20% over the next 6 months, with high volatility
Sector Rating	Remark
Overweight	Relative performance over Hang Seng Index $\geq 10\%$
Neutral	Relative performance within Hang Seng Index -10% to +10%
Underweight	Relative performance below Hang Seng Index $\leq -10\%$

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