



8 January 2014 | 9 pages

Auto Manufacturers

Asia | China

China Harmony Auto (3836.HK)

Analyzed Non-Rated Snapshot

- Company Overview** — China Harmony is an automobile dealership group headquartered in Henan province. It operates 28 dealerships with 9 ultra-luxury and luxury brands and two associate stores as of the end of 1H13. The brands include BMW, Lexus, BMW MINI, Rolls-Royce, Aston Martin, Jaguar, Land Rover, Ferrari, Maserati and Audi (minority interest). More than 60% of the stores are in Henan Province. BMW, Lexus and MINI are three major brands that accounted for 99% of total volume (BMW 86%, Lexus 10% and MINI 3%) in 2012. China Harmony has no mass-market brands in operation. Approximately 90% of total revenue is from new car sales and ~10% is from after-sales services. About 70% of gross profit is from new car sales and ~30% is from after-sales services.
- Business Strategy** — China Harmony's strategy is to lease land at primary locations for new outlets instead of acquiring land use rights. This strategy enables it to have comparatively lower capital expenditure for new outlets, thus China Harmony has a higher margin compared with some other dealers during the first few years when rent is relatively low. China Harmony also intends to establish multi-brand after-sales service centers and used car business starting operation in 2H13.
- Recent Results** — Overall 1H13 sales were Rmb3,659mn (+24% y-y) with Rmb3,345mn from new car sales, which is 91% of total revenue. After-sales market revenue was Rmb314mn, +21% y-y, 9% of total revenue. New car sales volume was 7,038 units in 1H13 (+30% y-y). 1H13 net income was Rmb251m (+52% y-y). 1H13 gross profit margin was 12.8% (11.9% in 2H12 and 11.6% in 1H12), and net margin was 6.9% (6.9% in 2H12 and 5.6% in 1H12). China Harmony ASP declined 7% y-y, but increased 5% h-h in 1H13.
- Strengths** — 1) China Harmony believes its strategy of leasing land at primary locations for new stores instead of acquiring land use rights enables it to control initial capex and maintain good margin. 2) As a dealership specializing in premium brands, the company has extensive coverage of the most well-known ultra-luxury and luxury brands and it also plans to add the Volvo brand.
- Weaknesses** — 1) Although its scale is already relatively large, it is still not as comparable as some industry-leading dealership groups like Zhengtong or Baoxin. 2) The specialization in luxury and ultra-luxury may make China Harmony vulnerable to unfavorable economic conditions.

Price (07 Jan 14)	HK\$5.43
Shares Outstanding	1,094M
Free Float (%)	64
Fiscal Year End	31 Dec
Market Cap	HK\$5,931M
	US\$765M

Price Performance

(RIC: 3836.HK, BB: 3836 HK)



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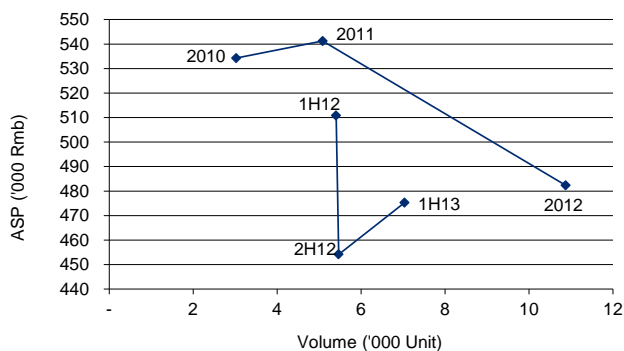
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Figure 1. China Harmony – Income Statement

P&L (RmbM)	2010A	2011A	2012A	1H12	2H12	1H13
Sales	1,801	3,032	5,657	2,952	2,705	3,659
y-y growth %		68.3%	86.6%			24.0%
Cost of sales	(1,570)	(2,614)	(4,993)	(2,611)	(2,383)	(3,192)
Gross profit	231	418	663	341	322	468
GP margin %	12.8%	13.8%	11.7%	11.6%	11.9%	12.8%
y-y growth %		80%	59%			37%
Other income	24	79	237	76	161	168
Selling & distribution cost	(65)	(107)	(237)	(109)	(128)	(165)
Administrative expenses	(19)	(30)	(72)	(27)	(44)	(45)
Other expenses	-	-	-	-	-	-
EBIT	172	359	591	281	311	426
EBIT margin %	9.5%	11.9%	10.5%	9.5%	11.5%	11.7%
y-y growth %		109%	65%			52%
Financial cost	(20)	(62)	(116)	(60)	(57)	(82)
Share of JV/associate	-	-	0	-	0	0
Profit before tax	152	297	475	221	254	344
Income tax	(39)	(77)	(125)	(57)	(68)	(95)
Minority interest	-	0	0	0	(0)	1
Net income	113	220	351	165	186	251
Net margin %	6.3%	7.3%	6.2%	5.6%	6.9%	6.9%
y-y growth %		96%	59%			52%

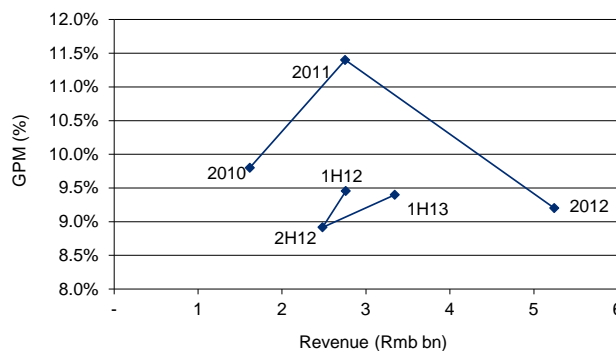
Source: Company Reports

Figure 2. China Harmony - New Car Sales Volume & ASP



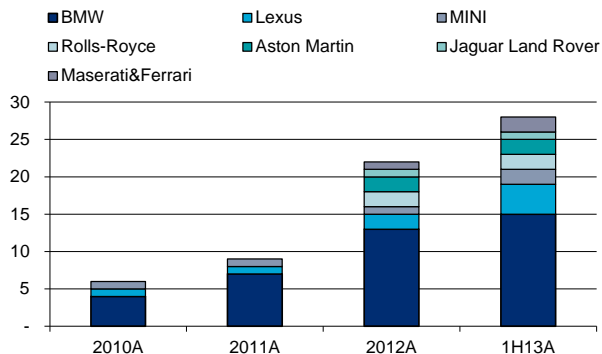
Source: Company Reports

Figure 3. China Harmony - New Car Sales Revenue & GPM



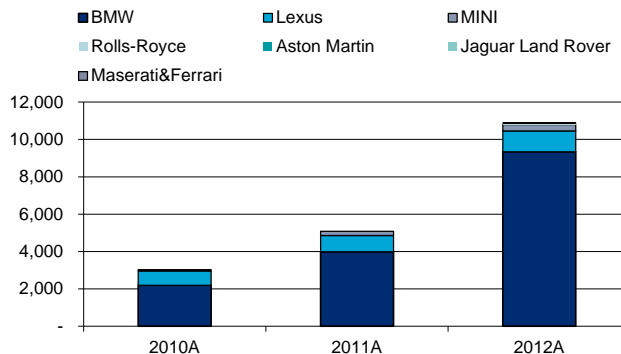
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Figure 4. China Harmony - Number of Stores Breakdown



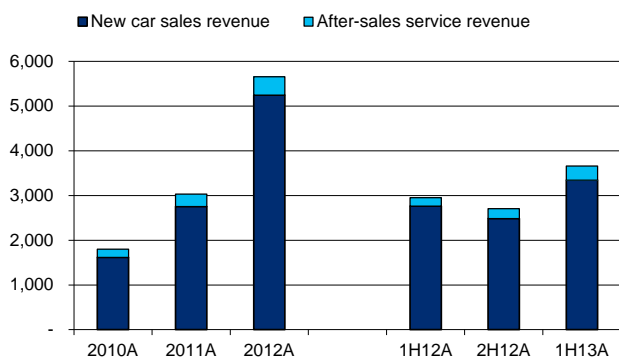
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Figure 5. China Harmony - New Car Sales Volume Breakdown



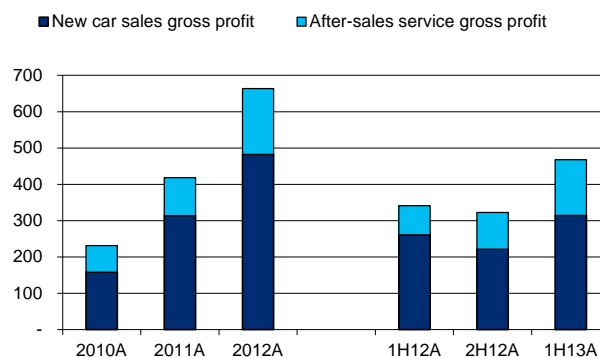
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Figure 6. China Harmony - Revenue Breakdown (Rmb mn)



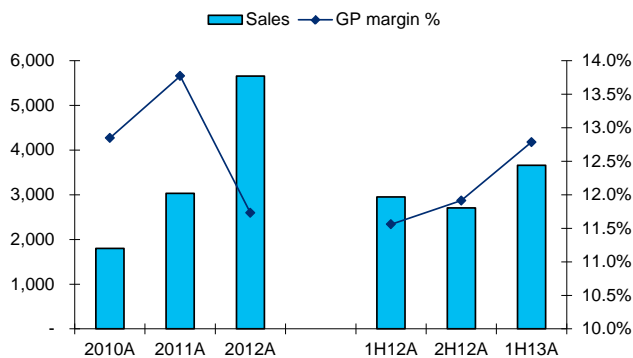
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Figure 7. China Harmony - Gross Profit Breakdown (Rmb mn)



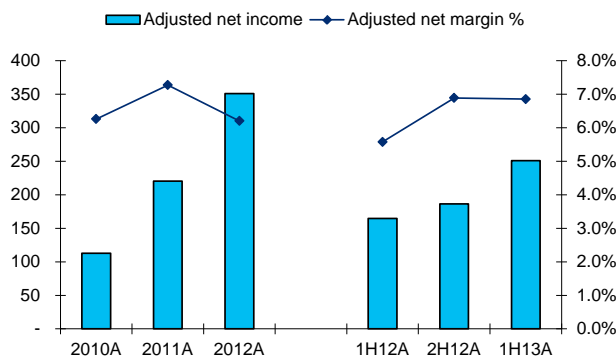
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Figure 8. China Harmony - Sales (Rmb mn) & GP Margin (%)



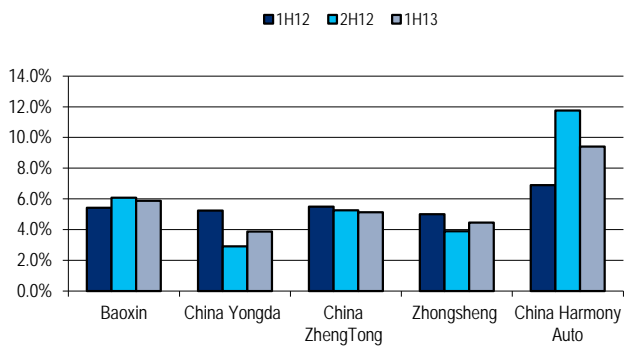
Source: Company Reports

Figure 9. China Harmony - Net Income (Rmb mn) & Net Margin (%)



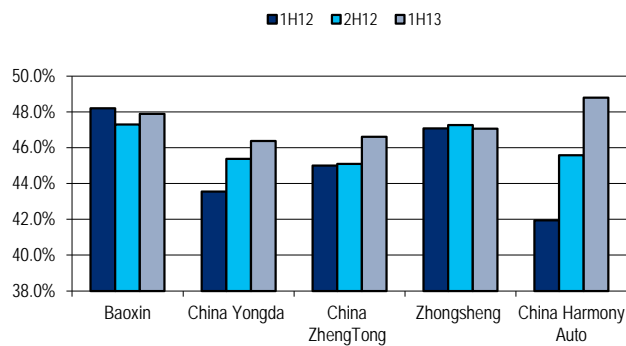
Source: Company Reports

Figure 10. China Dealers – New Car Sales GP Margin Comparison



Source: Company Reports, Citi Research

Figure 11. China Dealers – After-sales Services GP Margin Comparison



Source: Company Reports, Citi Research

- **Industry Overview** — After-sales service is the key growth driver for auto dealerships, as currently the ownership base is growing even faster than new car sales growth in China. New car sales margins are the key cyclical factor for dealership profitability. In 2013, over 20mn autos were sold in China, making it world's biggest auto market.
- **Competitive Analysis** — Major competitors are auto dealerships having similar brands and locations. They compete with each other for manufacturer's authorization, store locations, customer base, employees, etc. Competitors of auto dealerships also include both same-brand dealers and dealerships of competing auto brands.

Appendix A-1

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