CHINA TONGHAI SECURITIES 中國通海證券

Differ Group

Forge ahead in auto e-commerce

Initiation of coverage

We initiate coverage on Differ Group (Differ) with a Buy rating and 12-month SOTP-derived target price of HK$3.51. We believe Differ offers investor exposure to the booming China's auto consumer market. In August 2021, the company established an integrative auto e-commerce ecosystem, namely Cherries Car (车厘籽汽车), to provide comprehensive auto solutions and services to a wide range of customers. It is expected to contribute to the Group's growth trajectory (47.1% of total revenue in 2023E, segment profit of RMB13bn in 2023E). We view current valuations (6.9x 2023E P/E) as attractive relative to peers, given its robust O2O auto business prospects. Our 12-month PT implies a potential upside of 45.8% to current levels.

Company description

Differ started as an integrated financing service provider, mainly providing short to medium-term financing for SMEs in China and engaging in asset management business with financial licenses. It recently expanded into O2O auto platforms, forming Cherries Car through M&A and strategic partnership with multiple leading auto industry players. Cherries Car involves B2C & B2B auto transactions, auto financing, component supply, and marketplaces, etc. and its customers range from car manufacturers, car dealers to retail consumers.

Outlook

We expect Differ to capture the ample opportunities in the burgeoning China auto e-commerce market, propelled by the strong demand for auto-related services due to NEV sales and the structural shift of car buyers' behaviour to online. Its comprehensive O2O auto ecosystem is expected to rapidly penetrate the market, with enhancing synergies and rapid expansion with M&A and partnerships with leading auto industry players.

Catalysts

(1) Faster-than-expected acquisitions of industry-leading players; (2) Incremental growth of China's auto consumer market triggered by NEV replacement trends; (3) Growing demands for auto financing for used car transactions with easing regulatory restrictions.

Valuation

Our 12-month SOTP-derived target price for Differ of HK$3.51 implies 10.1x 2023E P/E and is at a similar valuation compared to its O2O auto business peer's 10.3x. We believe its forward P/E target is justified, given its robust O2O auto business expansion (2023E segment net profit growth of 205 % y/y).

Key downside risks

(1) Intensifying competition from auto e-commerce players; (2) The failure to adapt to the rapid changes in China's auto value chain; (3) Fall in property value

Differ Group (6878 HK) Key Financials

(RMB'mn)	FY19	FY20	FY21E	FY22E	FY23E
Revenue	2,306	6,170	1,786	4,162	5,154
y/y growth	*161.9%*	*167.6%*	*(71.1%)*	*133.1%*	*23.8%*
EBIT	420	522	675	1,710	2,861
y/y growth	*4.5%*	*24.1%*	*29.5%*	*153.1%*	*67.3%*
Attributable profit	336	356	397	1,297	2,053
y/y growth	*15.5%*	*6.1%*	*11.6%*	*226.4%*	*58.3%*
Diluted EPS (HK$)	0.06	0.06	0.07	0.22	0.35
P/E (x)	37.1	37.8	35.8	11.0	6.9

Source: Company Data, China Tonghai estimates

China Auto

2 Mar 2022

Ticker	6878 HK
Stock Rating	BUY
Industry View	POSITIVE
Price Target (HK$)	3.51
Price (28-Feb-2021)	HK$ 2.41
Potential	46%
Upside/Downside	Upside
Market Cap (HK$mn)	17,372
Shares Outstanding (mn)	7,208
Free Float (%)	42.0
3M Avg Daily Turnover (HK$mn)	75
52 Week range	HKD 0.70– 3.84

Source: Bloomberg

China Auto

Tonghai Research

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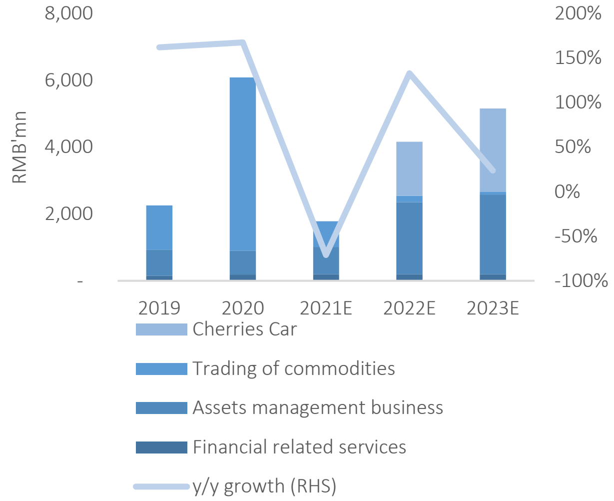
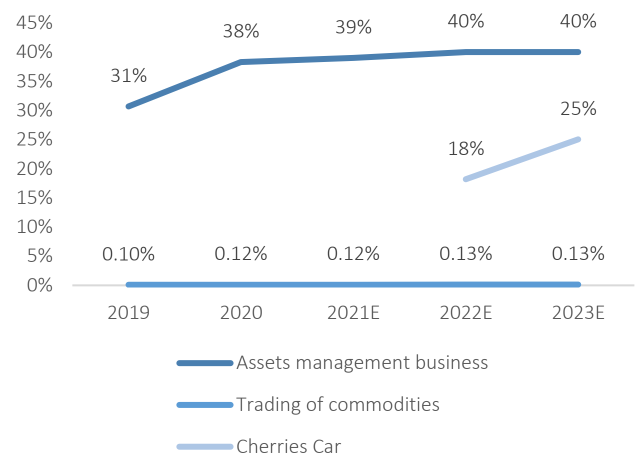
DIFFER GROUP – KEY CHARTS

Figure 1. Differ Group – Revenue by segment, 2019-23E



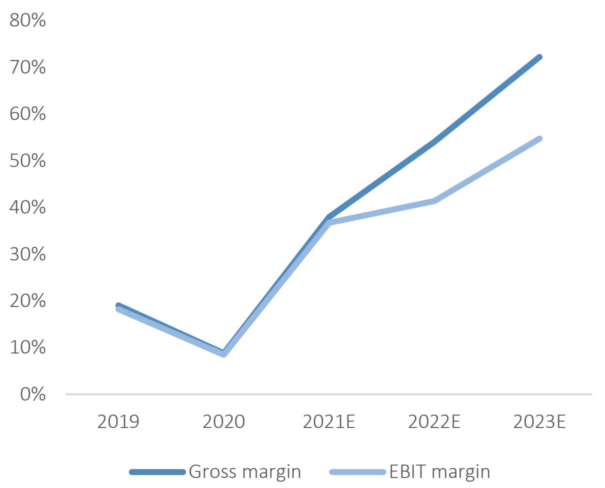
Source: Company data, China Tonghai Securities estimates

Figure 2. Differ Group – Gross margin by segment, 2019-23E



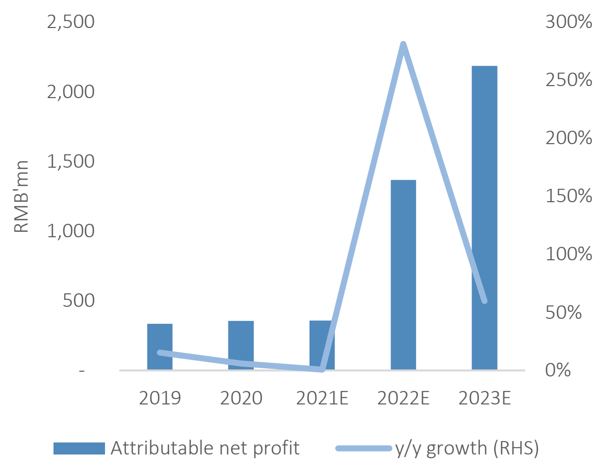
Source: Company data, China Tonghai Securities estimates

Figure 3. Differ Group – Gross margin and EBIT margin, 2019-23E



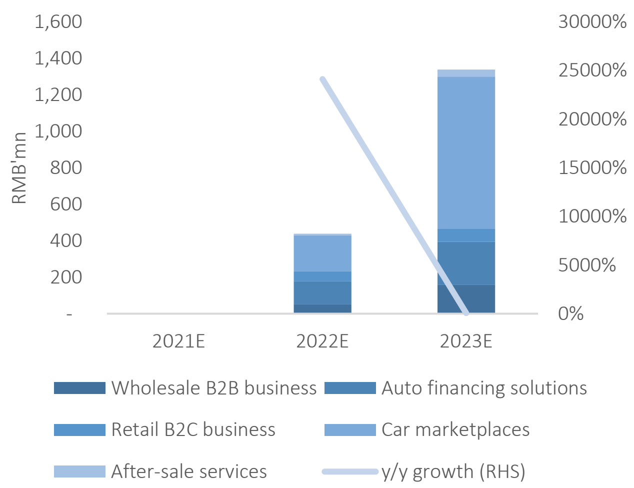
Source: Company data, China Tonghai Securities

Figure 4. Differ Group – Attributable net profit, 2019-23E



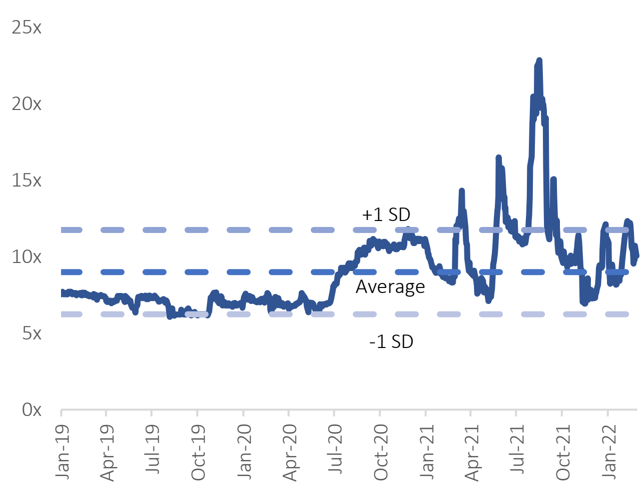
Source: Bloomberg, China Tonghai Securities estimates

Figure 5. Differ Group – Net profit mix in Cherries Car business segment, 2021-2023E



Source: Company data, China Tonghai Securities estimates

Figure 6. Differ Group – Forward P/E



Source: Company data, China Tonghai Securities estimates

KEY INVESTMENT VIEWS

We are positive about Differ Group's future outlook on the back of its robust growth momentum in the O2O auto business platform known as Cherries Car. It is expected to benefit from the booming China's auto consumer market and stand out in the market with a comprehensive O2O auto ecosystem with strong synergies and effectively addressing the industry pain points.

As a beneficiary of China's lucrative auto consumer market proliferation

Differ as a beneficiary of China's lucrative auto consumer market proliferation

Differ Group is poised to capitalize on China's automobile e-commerce market opportunities, driven by the ramp-up demand for auto services with a growing potential of car parc per capita, NEV replacement trends, and the increasing maturity of new retail auto business models.

The incremental potential of car parc per capita: We expect the incremental potential of car parc per capita sparked by China's stable GDP growth and increasing consumer power will support the new auto sales initially and used car market expansion gradually as the car parc is getting higher. Compared to developed countries (US: 85 car parc per 100 people in 2020), China's car parc per capita is relatively low (20 car parc per 100 people during the same period), signaling large growth room and market opportunities for China's auto industry players.

NEV replacement trends stimulating the demand for auto-related services: We believe the rapid NEV penetration (with a 2013-20 CAGR of 85.6% in sales volume) with technology advancement and solid policy support will stimulate the auto consumer market expansion and the demand for auto-related services across the value-chain.

The structural shift of auto consumer behavior to online spurs the demand for e-commerce auto marketplaces and calls for a sophisticated O2O model that bridges the existing gap between online and offline channels.

Ongoing acquisitions and partnerships accelerating its market share expansion

The ongoing partnerships and acquisitions drive a broader array of products and services

We expect the ongoing acquisitions and partnerships with leading industry players in the near term to broaden the array of Cherries Car's products and services, ultimately propelling the strong business growth momentum (2023E segment net profit growth of 205 % y/y) and accelerating its market share expansion. It will drive multiple lucrative businesses pipeline and empower Cherries Car with rich business resources and expertise.

Enhancing integration within the O2O auto ecosystem drives incremental growth

The enhancing synergies within Cherries Car as an integrative O2O auto ecosystem is expected to foster the overall auto business expansion on the back of the wider application of big data, increasing economies of scale and stronger bargaining power across the value chain.

Synergies with the existing financial business

The growing synergies within the financing business will solidify its auto business

We believe the deepening integration with its traditional financial businesses is set to usher in the growth momentum for its diversified O2O auto financing services, involving supply chain financing and auto loans.

We see a solid foundation for its financing business on the back of 1) a sophisticated business network, 2) a well-developed risk-control system, 3) rich experience in financial operation, and 4) a large-scale line of credit (LOC) and capital.

In addition, the solid policy support for auto financing to boost domestic NEV sales and the growing auto financing demand from used car transactions will also act as a prospectus.

Initiate at Buy with a 12-month TP of HK$3.51

We initiate coverage on Differ Group with a Buy rating and a 12-month TP of HK$3.51, implying a target 2023E P/E of 10.1x. We believe Differ Group is a key beneficiary of China’s burgeoning auto e-commerce space. We consider its current valuation of 6.9x 2023E P/E attractive, given its strong growth momentum in the O2O auto business (with a segment profit of RMB1.3bn in 2023E).

Key risks

The key downside risks for Differ Group include 1) Slower-than-expected O2O auto business expansion due to intensifying industry competition and lack of operation experience will cast a shadow on the market confidence in its new business; 2) The rapid changes in the China auto value chain with the penetration of NEV may bring uncertainties to its O2O auto business.

COMPREHENSIVE AUTO E-COMMERCE ECOSYSTEM STRATEGY

Comprehensive auto e-commerce ecosystem strategy to address different pain points in the value chain

We believe the newly established Cherries Car will be the driver for Differ's business growth momentum. It captures the opportunities in the booming post-pandemic China's auto consumer market with a comprehensive O2O auto ecosystem that involves different sub-businesses developing synergies.

Diversified products portfolio covering across the value chain

Differ Group established an e-commerce ecosystem through M&A and strategic partnerships and named it Cherries Car (车厘籽). It first integrated Maimaiche (买卖车), an app product for wholesale B2B business, to the ecosystem, after acquiring Qiancheng Taifeng Technology (乾程泰锋) for RMB53mn in August 2021.

Cherries Car consists of 5 app products targeting different auto O2O value chain segments, including transaction (B2B&B2C), financing, manufacturing, and auto component supply and serving consumers, dealers, OEMs, etc.

That include **1) Maimaiche (买卖车)** - Wholesale B2B (auto dealers) business; **2) Chezhixiao (车智销)** - Retail B2C business; **3) Chejinfu (车金服)** - Auto financing solutions; **4) Smart Marketplace (智慧卖场)** – Car marketplaces; and **5) Cheshifu (车师傅)** - After-sale services.

Fig 7. Cherries Car product portfolio

Source: Company data

Cherries Car is expected to capitalize from adding value to the auto e-commerce value chain and appeal to a broader user base by effectively addressing their different needs.

Fig 8. Cherries Car – Key value adds to the existing auto market value chain

Products	Business model	Targeted Pain Points	How the product adds value
Maimaiche（买卖车） 	Facilitates transactions among car dealers It charges 1) **membership fees** for providing quotation prices from different dealers, 2) **services fees** for procurement, consignment sales and group buying, and 3) **delivery fees** for trans-regional transactions delivery services	**Overstocking inventories** for car dealers due to over-purchase from manufacturers	– Integrates Chezhixiao to enable car dealers to base demand on procurement （以销定采） with consumer data – Ultimately allows auto manufacturers to base the order on production (以销定产)
		High frictions in the B2B car dealers transactions	– Reduces financial risks in the transactions with secure payment and financing services – Provides trans-regional delivery services with delivery centers across the country
Chezhixiao （车智销） 	Matches car dealers with interested users by aiding advertisers in designing and releasing CPA (cost per acquisition or action)-based ads in the traffic platforms based on users' searches and the potential demand It charges **commission fees** as a proportion of the transaction value per unit.	**Low effectiveness** in the marketing services provided by major traffic platforms for auto brokers	– Provides customized targeting marketing solutions for auto brokers to converse the traffic to the consumers effectively and matches consumers with auto brokers based on their search flows – Facilitates B2C transactions by leading consumers to the self-developed car delivery centers and car marketplaces
Chejinfu （车金服） 	Provides supply chain financing for car dealers and auto loans for retail consumers in the deals and supports car transactions with secured payment services. It charges **interest and service fees** from the services.	The existing financing products failed to satisfy diversified auto financing needs	Provides one-stop auto financing solutions with a well-developed business network with financial institutions, a large-scale LOC, and a high-quality risk control system
Smart Marketplace （智慧卖场） 	Provides offline showrooms, storage, and promotion activities to promote car transactions and complements B2B2C online sales solutions It charges fees as a percentage of the transaction value.	The **idleness** of existing car marketplaces with poor property management	Integrates self-developed and existing idled car marketplaces with e-commerce platforms to boost B2B and B2C transactions

Cheshifu (车师傅) 	Offers car components supply-chain services for maintenance and insurance claim settlements It charges fees as a proportion of the transaction value for procurement and a percentage of the total auto parts and components value for claims settlements.	The **high maintenance costs** in the after-sales services for consumers	Matches the proper car maintenance companies for consumers with highly cost-effective services for claim settlements and boosts the sales for car maintenance companies accordingly
		Less-developed supply chain system for some car maintenance companies	Empowers some car maintenance companies calling for a well-developed auto-component supply network and save their supply chain costs

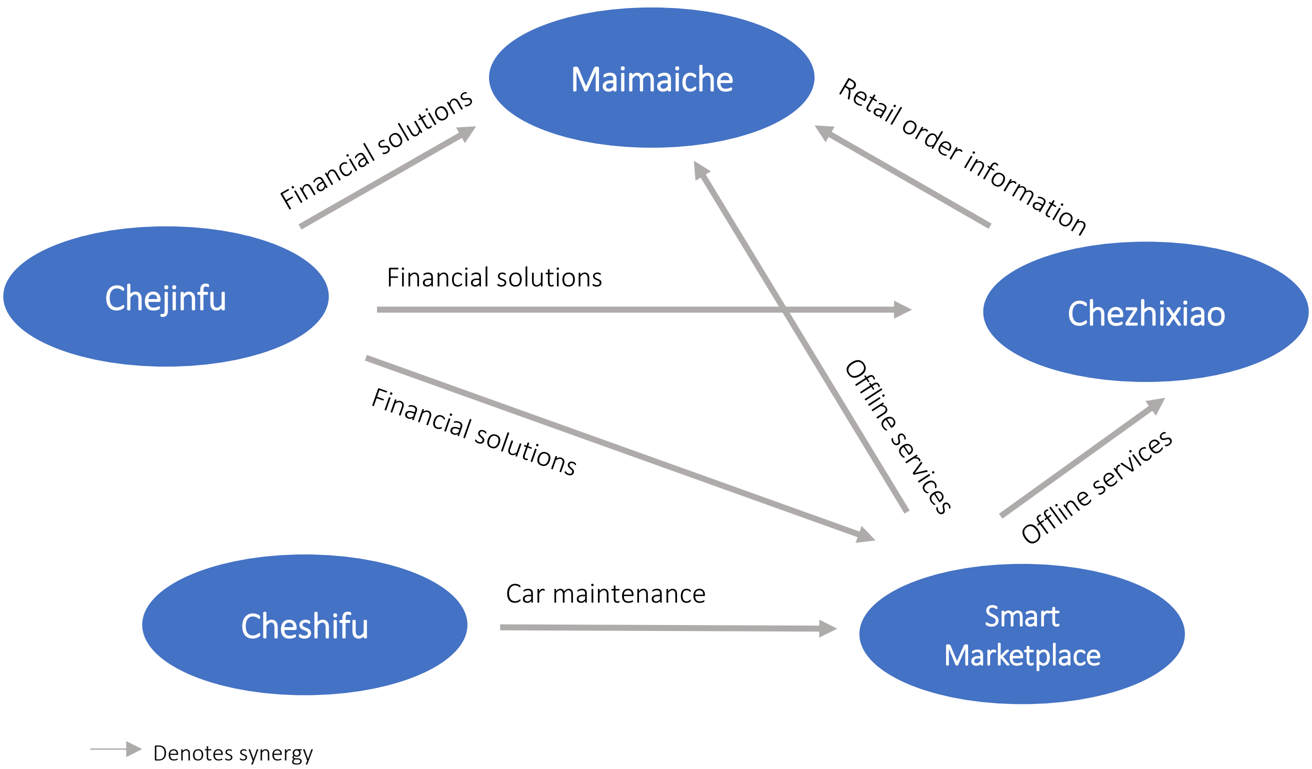
Source: China Tonghai Securities

Synergies within the O2O auto ecosystem

The five businesses of Cherries are inter-connected and achieve synergy effects

The five businesses are inter-connected, creating synergy effects. They benefit from Cherries Car ecosystem with resources sharing, higher operating efficiency, and economies of scale. For example, Chejinfu contributes to Maimaiche and Chezhixiao with financial support for dealers and retail consumers. Chezhixiao provides Maimaiche with retail order information so that dealers can procure based on sales. Smart Marketplace integrates Maimaiche, Chejinfu, and Chezhixiao to complement online platforms with offline services.

Fig 9. Cherries Car – Synergies within the ecosystem



Source: China Tonghai Securities

INTEGRATION WITH LEADING INDUSTRY PLAYERS

Partnerships as solid support for Cherries Car

The acquisitions and strategic partnership removed the roadblocks

Cherries Car has established partnerships with leading industry players, such as Sichuan Zhuzi Automobile, Audi, Xpeng, etc., after it acquired Qiancheng Taifeng Technology in August 2021. Its strategic partners include auto manufacturers, auto financing service providers, advertisers, auto e-commerce platforms, etc.

We believe the acquisitions and strategic partnership removed the roadblocks for Differ Group as a new entrant and enabled the company to capture the market opportunities promptly. The industry-leading auto business resources and expertise brought by the acquired and partnered leading industry players will provide solid support for its O2O auto business development.

Fig 10. Cherries Car partnership network

Source: Company data

Ongoing acquisitions chalk up inorganic growth

Going forward, Differ Group plans to acquire some of its strategic partners to have better control and restructuring over their businesses. We expect the ongoing acquisitions to improve its products and accelerate its inorganic growth. For example, the potential acquisition of 1) Shanghai Internet e-Commerce (上海网商) is expected to benefit Chezhixiao with more sophisticated targeting marketing solutions and 2) Sichuan Zhuzi Automobile (竹子买车) is expected to expand the Smart Marketplace’s geographical landscape.

Fig 11. Differ Group– List of latest acquisition targets in the MOU (memorandum of understanding)

Acquisition targets	Description	Implications
Shanghai Internet e-Commerce(上海网商)	Provides comprehensive marketing solutions for auto and component sales in e-commerce platforms such as Tmall	Brings **Chezhixiao** a strong network of auto manufacturers, dealers, and retail consumers and sophisticated targeting marketing solutions
Tianjin Mashang Haoche Information Technology (马上好车)	Provides financing, storage (with over 400 warehouses in over 100 cities), and logistics services for auto dealers and manufacturers via an online platform	Improves the auto financing services portfolio for **Chejinfu**
Sichuan Zhuzi Automobile (竹子买车)	Offers a wide range of autos and auto financing to consumers through its online platform (Bamboo Buy a Car 竹子买车)	Expands the **Smart Marketplace**'s geographical landscape to southwestern areas from northeastern regions and extends the auto financing network

Source: Company data

SYNERGIES WITH EXISTING FINANCIAL BUSINESS

Solid foundation in financing services

Its sophisticated operation in auto financing lease service underpins the O2O auto business

Differ started as a financial services provider which addresses short-medium financing needs of small-medium enterprises and disposes distressed assets from state-owned financial institutions.

Its sophisticated operation in auto financing lease services and management's rich experience in parallel-import cars business underpin 1) its deep understanding of the auto and auto financing market, 2) big data-based risk management system, and 3) well-established business network with regional auto dealers and financial institutions.

Rich experience in project acquisitions and integration

Its asset management experience will lead to a better strategic alignment among different acquirees

The company's rich experience in project acquisitions and integration from asset management business will lead to a better strategic alignment among different acquirees and strategic partners in the auto market.

Differ Group has fully engaged in different phases of project operation in its asset management business, ranging from acquisition, integration/development/renewal, to sales. We expect its leading investment insights and financing experience in its asset management business will benefit its O2O auto business by enabling the company to select promising and proper industry players to partner with and finance the new projects efficiently.

AMPLE OPPORTUNITIES IN CHINA'S AUTO CONSUMER MARKET

We expect Differ's Cherries Car to capitalize on China's lucrative auto consumer market proliferation, supported by the NEV replacement trends, used car market expansion, a structural shift of China's auto consumer behaviour to online.

Robust auto consumer market growth

We believe the robust auto consumer market growth will support Cherries Car business expansion, with increasing demand driven by the NEV replacement trends and used car sales growth.

NEV replacement trends drive the China's auto consumer market demand

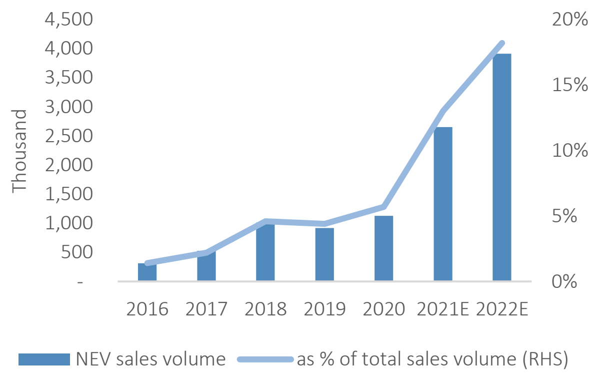
The proliferating NEV market to drive the China auto consumer business expansion

In recent years, China's NEV sales volume registered a robust growth pattern defying the auto market downturn. We expect the proliferating NEV market with solid policy support and rising market recognition to drive China's auto consumer business expansion by stimulating the demand for auto-related services.

YTD Nov 2021, c.2.5mn NEVs were retailed in China, surging 178.3% y/y, while the overall auto sales volume showed slower growth of 6.1% y/y. The NEV penetration rate during the period increased to 13.9% (from. 5.8% in 2020) . According to State Council's target, the total sales volume of NEVs will account for 20% of the overall by 2025E.

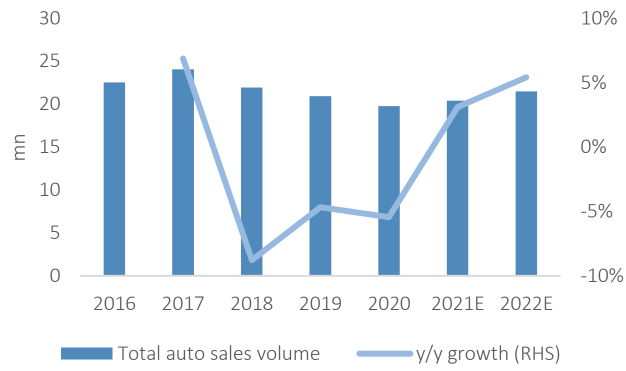
We expect NEV penetration to expand, with increasing market maturity after the gradual withdrawal of subsidies, enhancing technology know-how of NEV developers, expanding charging station infrastructure, and easing supply chain shortage. The NEV replacement trends usher in demand for higher quality services across the auto value chain.

Figure 12. China NEV sales volume and penetration, 2016-2022



Source: China new car insurance registration database, CAAM, China Tonghai estimates

Figure 13. China total auto sales volume and y/y growth, 2016-2020



Source: China new car insurance registration database, CAAM, China Tonghai estimates

Potential of the used car market usher in auto e-commerce penetration

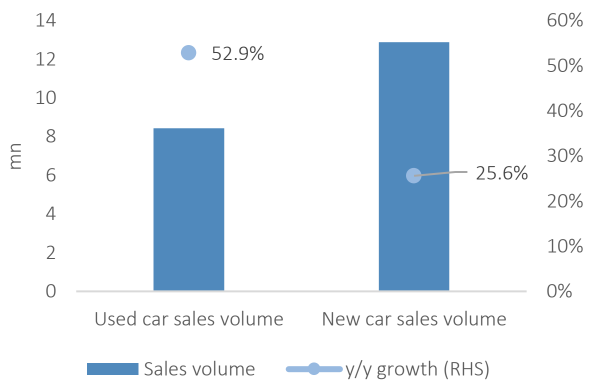
The unleashing potential in the used car market to usher in auto e-commerce penetration

The used car market saw rapid growth post-pandemic, and the ratio of new cars to used cars trading volume reached a historic high of 0.83, as the chipset supply shortage impeded the delivery of new cars and shifted the demand to used cars. We expect the potential of the used car market to unleash, on the back of increasing consumer acceptance, especially among Z generation consumers (born in 1995-2009), and the removal of regulatory restrictions and lower value-added tax taxation over the used car transactions.

It will ultimately usher in the rapid expansion of used car marketplaces and e-commerce penetration. The e-commerce model can contribute to the used car market by addressing information asymmetry effectively and aiding fairer pricing and after-sale assurance.

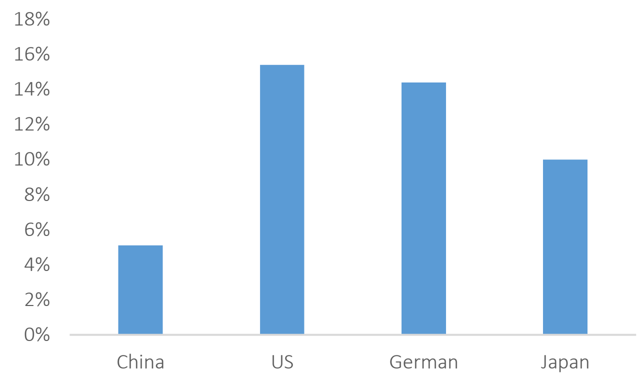
China saw large growth room in the used car transactions as car par increases. According to China Automobile Dealers Association, the trading volume of used cars in the China market is likely to reach the level of new car sales volume by 2025E.

Figure 14. The comparison between China new car and used car sales volume and y/y growth in 1H21



Source: China Automobile Dealers Association

Figure 15. Selected countries' used car trading volume as of car parc (%) in 2020



Source: Ministry of Public Security, Auto Nation

New retail formats spurred by the pandemic

We believe Cherries Car as a comprehensive O2O auto solution provider to monetize from the growing popularity of the new retail business model in the auto market after the pandemic and addressing the existing pain points in the burgeoning O2O auto space.

The structural shift of auto consumer behaviour to online

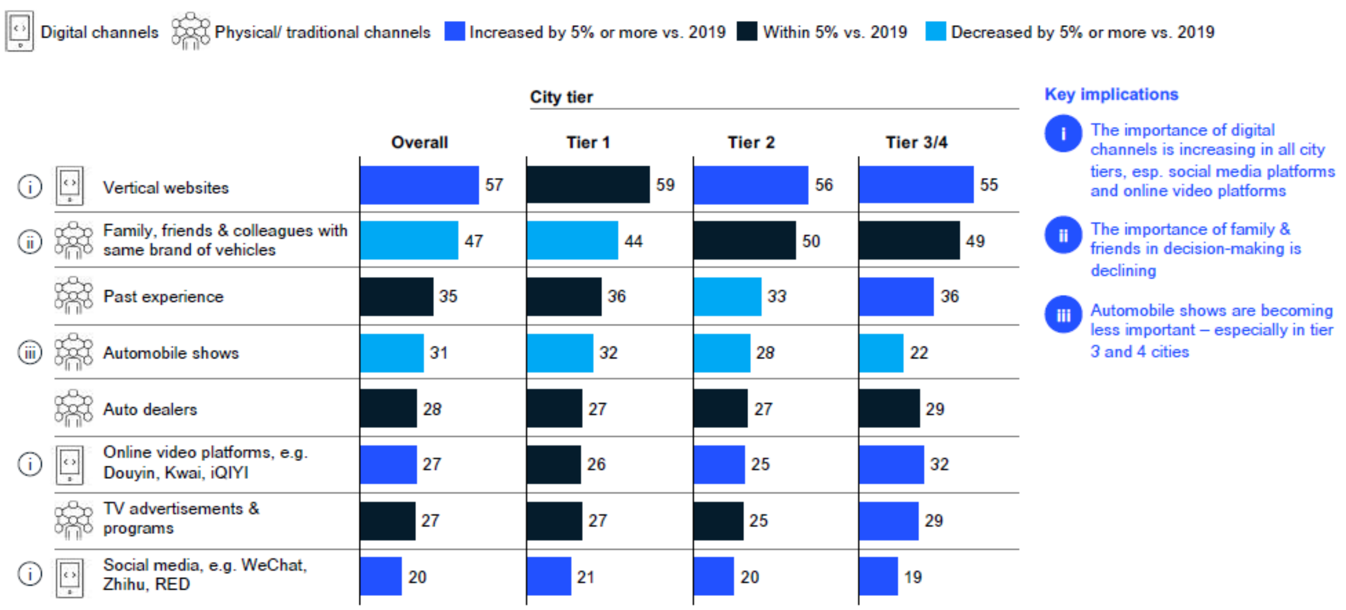
New retail formats post-pandemic call for auto O2O solutions providers

Digital channels, including auto vertical websites, online video platforms, and social media networks, are playing more important roles in information-gathering in the auto consumer's decision-making journey, endangered by the tightening social-distancing measures in the pandemic. This structural trend is expected to persist, as the digital channels eliminate information asymmetry to a large extent, and social media and live-streaming platforms have amassed enormous traffic and penetrated faster to all walks of life.

We believe this will spur the shift of marketing campaigns from OEMs and dealers to live-streaming and online social media, ultimately creating opportunities for auto online marketing solutions providers.

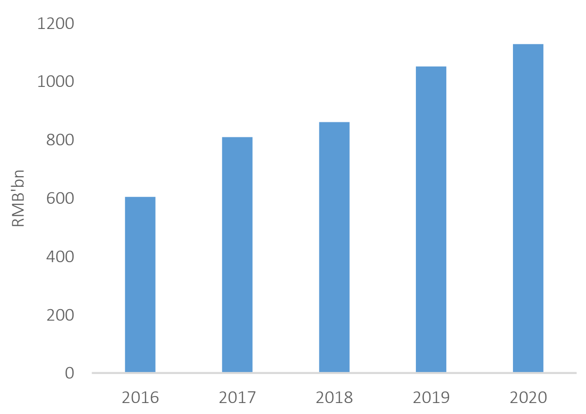
In addition, we expect China's well-developed e-commerce marketplaces to involve the auto business in the future to some extent with 1) the improving O2O model, 2) increasing preference for direct interaction with OEMs via online orders, and 3) the high popularity of online shopping among China consumers. According to WJS (网经社), China's automobile e-commerce market has reached RMB1.13tr in 2020, on the back of a large user base of around 185mn (2016-2020 CAGR: 39.4%).

Fig 16. Key channels for passive auto information acquisition, % of respondents, 2021 vs. 2019



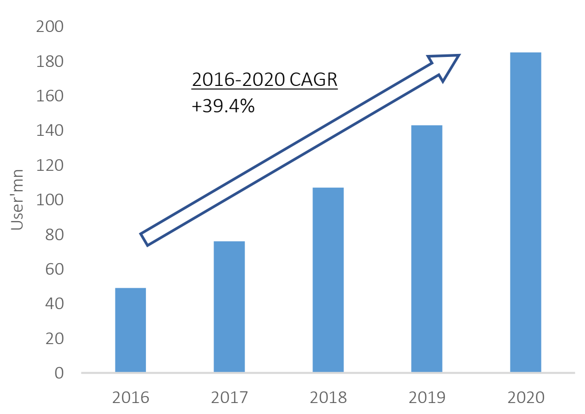
Source: 2019, 2021 McKinsey China Auto Consumer Insights

Figure 17. China auto e-commerce market size, 2016-2020



Source: WJS, China Tonghai Securities

Figure 18. China auto e-commerce user base, 2016-2020



Source: WJS, China Tonghai Securities

The gap between online and offline channels as industry pain points

The barriers between online and offline channels and information asymmetry across OEMs, dealers, consumers, marketing agencies, media, etc., call for a comprehensive O2O ecosystem to bridge the gap in big data and enable OEMs and dealers to react promptly to the market.

DIFFER GROUP – SEGMENT DRIVERS AND FORECASTS

In the following section, we outline our forecasts for Differ Group's core segments – Cherries Car and existing businesses.

Cherries Car (48.2% of 2023E revenue)

Outlook

Earlier investment and development will drive robust growth

We expect significant y/y increases in the profits across the board as its earlier investment and development efforts bear fruit, and all 5 businesses put into operation and rapidly penetrate the auto e-commerce market.

Forecast

Cherries Car: We forecast segment revenue CAGR of 1810.2% in 2021-23E and the business to account for 48.2% of total revenue in 2023E (vs 0.4% in 2021E), mainly driven by inorganic growth with ongoing acquisitions and partnerships with leading industry players and geographical expansions with the addition of car marketplaces franchisees.

- Wholesale B2B business: We forecast the wholesale B2B business net profit to grow 208% y/y to RMB157mn in 2023E (accounting for 11.7% of the segment profit), supported by the increasing membership fees and growing consignment sales for large car dealers. We assume 1) membership fees of RMB10,000 p.a, 2) services fees as 0.5% of the dealing price, and 3) delivery fees RMB2,000 per unit.

- Auto financing solutions: We forecast the auto financing solutions net profit to rise 87% y/y to RMB237mn in 2023E (taking up 17.7% of segment profit), driven by the growing loan amount of the diversified financing products and stable interest rates on the back of a large LOC. We assume service fees of RMB150 per unit for supply chain financing services and RMB500 per unit for retail financing services.

- Retail B2C business: We forecast the retail B2C business net profit to grow 32% y/y to RMB73.2mn, with advertisers network expansion and the improving efficiency in boosting the B2C transactions through ads or search flows conversion. We assume the commission fee takes 0.5% of the transaction value per unit.

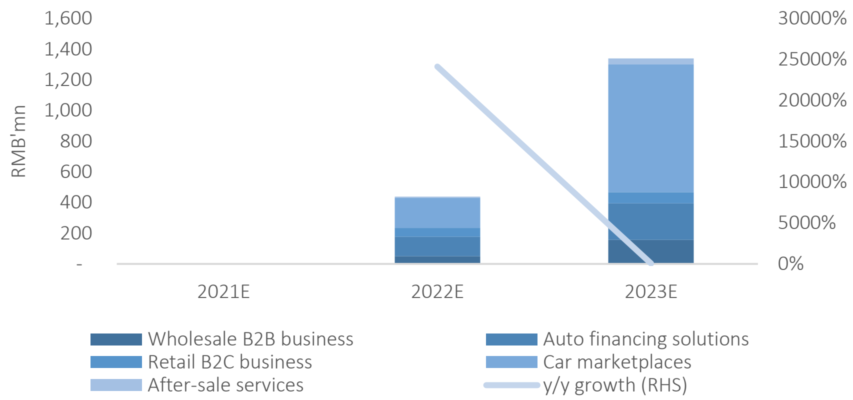
- Car marketplaces: We expect the car marketplaces business to be a significant growth driver for the O2O auto business. The segment profit is projected to jump to RMB832mn in 2023E (vs. RMB196mn in 2021E), contributing 62.1% of segment profit (vs. 44.7% in 2021E). The exponential growth will be backed by the increasing marketplaces franchisees and the boosted car transactions as a beneficiary of synergy effects with wholesale B2B business, retail B2C business and auto financing solutions, etc.

We assume it charges auto cities RMB10,000 p.d for promotion activities, RMB10,000 p.a. for app subscribing, and 40% of the advertising-generating profits.

- **After-sale services:** We forecast the after-sale services segment profit to increase 300% y/y to RMB40mn in 2023E, with the development in car components supply-chain network and the ongoing partnership with insurance companies. We assume it charges 2% of the transaction value for procurement and 6% of the total auto parts and components value for claims settlements.

Gross margin: We expect the segment gross margin to chalk up gradual and stable growth to 52% in 2023E (vs. 47% in 2022E), with economies of scale.

Fig 19. Differ Group – Net profit mix in Cherries Car business segment, 2021-2023E



Source: Company data, China Tonghai estimates

Existing businesses (51.8% of 2023E revenue)

Outlook

We forecast a stable financial-related services outlook, recovering asset management business and dwindling commodity trading business

We forecast a stable financial-related services outlook and dwindling commodity trading business as the company pivots to the O2O auto business. While its asset management business is expected to show recovery in 2022-23E, as its sold investment properties are delivered and recognized as revenue.

Forecasts

Financial-related services: We forecast financial-related services segment revenue CAGR of 1.7% in 2021-23E, with stable financial receivables scale and interest rates. We expect revenue contribution as a percentage of the total will decrease to 3.9% in 2023E (vs. 10.8% in 2021E).

Asset management business: We expect that asset management business will increase at 82.7% 2021-23E CAGR and account for 46.2% of revenue in 2023E (vs. 45.9% in 2021E), on the back of the foreseeable sold properties delivery and steady investment returns from properties development and distressed assets disposal.

Commodity trading business and others: We forecast the segment revenue CAGR of -66.5% in 2021-23E, with the company's gradual exit from the business and the drop in trading volume. We expect the revenue contribution as a percentage of the total will decrease to 1.7% in 2023E (vs. 42.9% in 2021E). We believe the contraction of the low-margin business (c. 0.1% in FY19-20) will contribute to overall profit margin expansion.

Description

Financial-related services: Differ Group provides short-medium financing solutions for mainly China Fujian-based small-medium enterprises which fail to get financial support from major financial institutions and charge for fees and interests from them.

Its diversified financing solutions include:

1) Guarantee services
2) Express loan services
3) Consultancy services
4) Finance lease services

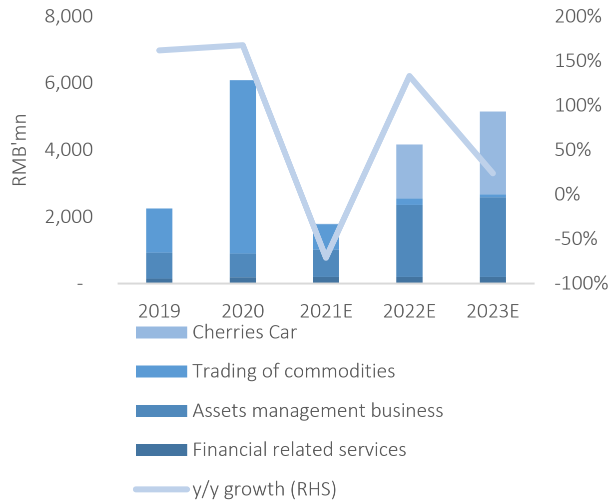
Asset management business: Asset management business comprises property development and investment, fund management, and distressed assets disposal.

To derive value from value assets, Differ Group entered the property development and investment business in 2015, focusing on historical and cultural tourism-related properties. It is fully engaged in different phases of project operation, ranging from acquisition, integration/development/renewal, to sales. And it monetized via generating incurring revenues from long-term leasing, exiting with sales, or financing with ABS.

It also involves **distressed assets disposal, equity,** and **fund investments** in Mainland China and Hong Kong. Its rich distressed assets reserves lay a solid foundation for the segment (distressed assets measured at FVOCI reached RMB94.8mn in 1H21, growing from RMB90.6mn in 1H20)

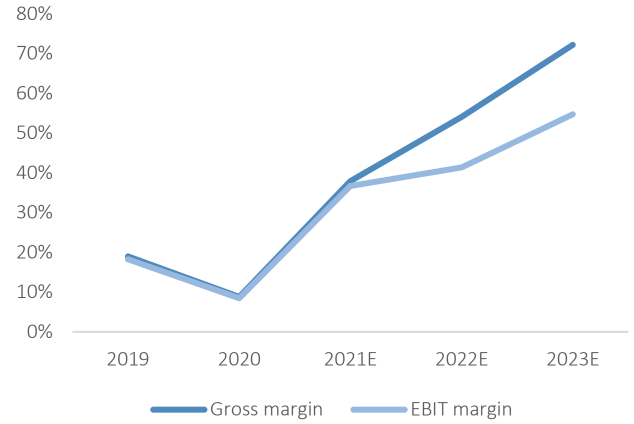
Commodity trading business: In the 1H19, the company transferred supply chain agency business (formerly belonged to financial-related services) to commodity trading business, where it purchases commodities from suppliers at a lower price and sells them to customers at a higher price.

Figure 20. Differ Group – Revenue mix by business segments, 2019-2023E



Source: Company Data, China Tonghai estimates

Figure 21. Differ Group – Gross margin and EBIT margin, 2019-2023E



Source: Company Data, China Tonghai estimates

VALUATION

We initiate coverage on Differ with a BUY rating with 12-month TP of HK$3.51. We believe Cherries Car's robust growth momentum (segment net profit y/y growth of 205% in 2023E) will strengthen market confidence and drive a rerating for Differ's shares. Our 12-month target 2023E P/E of 10.1x implies 46% upside potential.

Buy rating and 12-month TP of HK$3.51

Our 12-month price target for Differ Group at HK$3.51 in SOTP methodology, which we believe best reflects its intrinsic value. Our price target reflects our positive view for the rapidly expanding TAM in the auto e-commerce market and proliferation in its auto O2O business, and moderate growth in its financial-related services.

Target multiples for each segment

We arrive at our SOTP-derived TP of HK$3.51 by applying the following target multiples to the respective business segments:

- 11.9x 2023E P/E for Cherries Car, at a premium to its online auto platform peers' average of 10.3x 2023E P/E but below the intelligent platform peers' 15.6x. In our view, the valuation is justified by its above-average auto business growth and strong profitability

- 3.5x 2023E P/E for financial-related services and asset management business, at a premium to its financial peers' average of 2.6x 2023E P/E; in our view, the premium is justified by its large-scale and mature financial business supported by regional business network

- Factoring in the company's gradual exit from the commodity trading business (accounting for 1.7% of the total revenue in 2023E vs. 42.9% in 2021E), we do not apply a specific P/E multiple for the business.

Figure 22. Differ Group – SOTP valuation

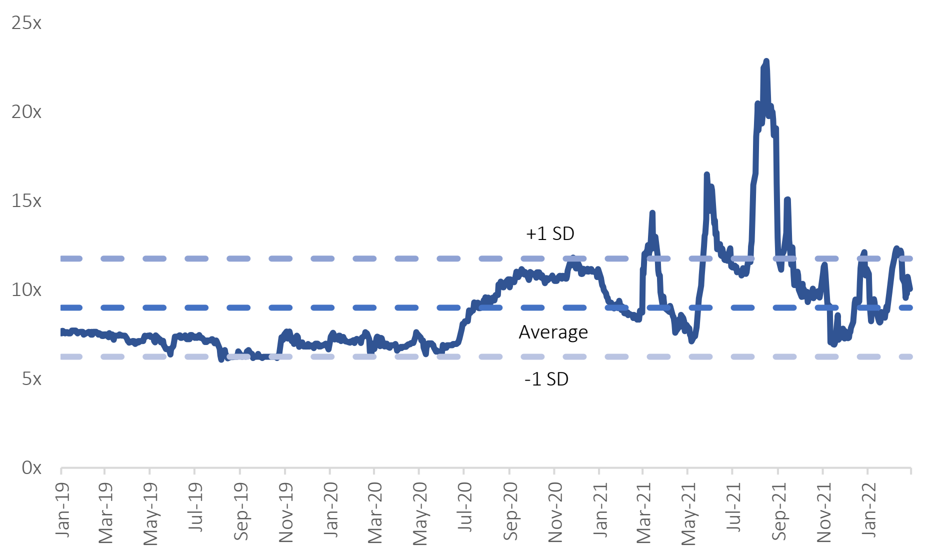
Business Segment	Valuation basis	Metrics	Assigned multiple	Segment as % of total	Valuation (RMB'mn)
Cherries Car	2023E P/E	2023E Segment profit RMB1,339mn	11.9	77%	15,939
Existing business	2023E P/E	2023E Segment profit RMB1,557mn	3.5	26%	5,451
Net cash	2023E			-3%	(627)
Total valuation					**20,763**
2023E adjusted net profit					2,053
Total basic shares (mn)					7,208
RMB-HKD					1.22
Target price (HKD)					**3.51**

Source: Company data, China Tonghai estimates

Share price trading pattern

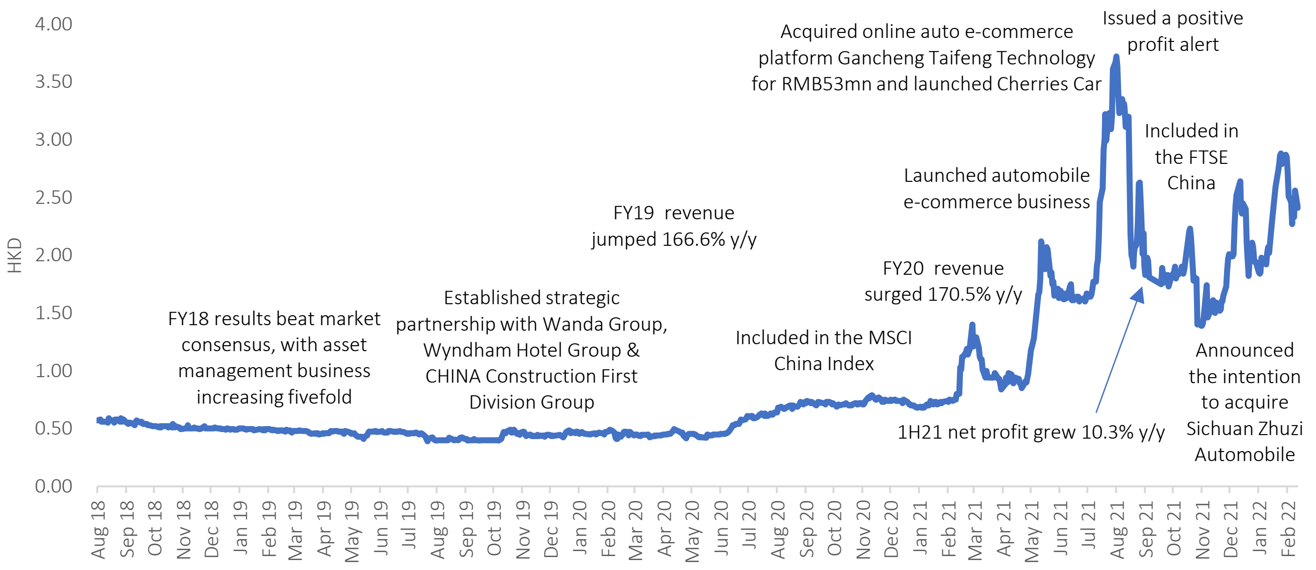
Following YTD share price decreased by 1.6% (versus HSI, which was down 2.4% during the period), the shares of Differ Group are trading at 10.1x weighted 2023E P/E, and above its recent 3-year average forward P/E of 9.0x.

Figure 23. Differ Group – Forward P/E



Source: Bloomberg, Company data, China Tonghai estimates

Figure 24. Differ Group– Key events and share price performance



Source: Bloomberg, Company data, China Tonghai Securities

Figure 25. Differ Group– Peer valuation comparable

				MktCap	3m Vol	EPS Growth (%)		P/E (x)		P/S (x)		ROE (%)		Ev/Ebit (x)		Net D/E (%)
Company Name	Ticker	Lcy	Price	US$bn	US$m	2022	2023	2022	2023	2022	2023	2022	2023	2022	2023	2020
DIFFER GROUP HOL	6878 HK	HKD	2.41	2	9	226.4	58.3	11.0	6.9	8.0	3.4	14.5	25.9	27.4	8.6	84
Financial Service																
CHINA CINDA-H	1359 HK	HKD	1.41	6.9	7	5.1	2.4	3.1	3.0	0.5	0.4	7.9	7.9	38.4	36.5	458
FIRST CAPITAL -A	002797 CH	CNY	6.36	4.2	67	(5.8)	15.8	-	-	7.6	5.6	(9.4)	(7.2)	-	-	(22)
CHINA HUARONG -H	2799 HK	HKD	0.41	4.2	10	-	-	-	-	-	-	-	-	-	-	1,558
KUNWU JIUDING -A	600053 CH	CNY	17.96	1.2	16	-	-	-	-	-	-	-	-	-	-	8
FINVOLUTION-ADR	FINV US	USD	4.19	1.2	6	(0.8)	11.7	3.2	2.9	0.7	0.6	21.3	19.8	1.7	1.5	(31)
HENGTOU SECURI-H	1476 HK	HKD	3.01	1.0	0	-	-	-	-	-	-	-	-	-	-	(32)
CHINA RENAISSANC	1911 HK	HKD	11.60	0.8	1	12.5	22.2	3.3	2.7	1.5	1.3	21.9	22.6	4.8	2.8	(12)
LEXINFINTECH-ADR	LX US	USD	3.59	0.7	8	(10.0)	12.2	1.9	1.7	0.3	0.3	26.6	24.1	2.4	2.7	139
				Average		0.2	12.9	2.9	2.6	2.1	1.7	13.7	13.4	11.8	10.9	258
O2O auto business																
SAIC MOTOR-A	600104 CH	CNY	18.11	33.5	142	14.6	29.6	7.2	5.5	0.2	0.2	10.3	10.6	7.8	7.0	14
AUTOHOME INC-ADR	ATHM US	USD	30.26	3.9	31	(21.9)	15.2	11.8	10.3	3.5	3.3	9.1	9.6	3.3	2.9	(77)
AUTOHOME INC-A	2518 HK	HKD	56.00	3.7	1	-	22.9	11.1	9.0	3.3	3.0	8.8	9.6	2.4	2.1	(77)
360 DIGITECH INC	QFIN US	USD	19.96	3.1	29	(1.6)	14.7	3.5	3.0	1.1	1.0	30.9	26.7	2.4	0.3	(45)
DADA NEXUS L-ADR	DADA US	USD	9.63	2.3	16	60.5	197.7	-	17.6	1.4	0.9	(16.7)	15.3	-	19.2	(76.1)
TONGDAO LIEPIN G	6100 HK	HKD	18.80	1.3	1	31.2	28.8	23.0	17.9	2.4	2.0	10.6	11.6	14.2	10.2	(76)
YIXIN GROUP LTD	2858 HK	HKD	1.17	1.0	1	128.6	3.8	11.8	11.4	-	-	-	-	-	-	51
ICLICK INTER-ADR	ICLK US	USD	2.73	0.3	2	2,337.5	91.3	14.0	7.3	0.7	0.5	7.4	10.5	26.9	9.4	(13)
CHINA FORDOO	2399 HK	HKD	0.56	0.1	2	-	-	-	-	-	-	-	-	-	-	58
CHESHI TECHNOLOG	1490 HK	HKD	0.65	0.1	1	-	-	-	-	-	-	-	-	-	-	(75)
				Average		364.1	50.5	11.8	10.3	1.8	1.6	8.6	13.4	9.5	7.3	(31)
Intelligent platform																
ZHEJIANG DAILY-A	600633 CH	CNY	9.45	1.9	73	13.6	16.0	18.9	16.3	3.0	2.5	7.3	11.8	10.2	(14)	7.3
GUANGDONG SOUT	300770 CH	CNY	45.98	1.7	60	18.3	14.0	13.4	11.8	6.4	5.6	19.8	10.1	9.0	(82)	19.8
SHANGHAI GANGL-A	300226 CH	CNY	42.59	1.3	25	31.5	30.0	22.4	17.2	0.1	0.1	18.4	17.6	13.5	116	18.4
TONGDAO LIEPIN G	6100 HK	HKD	18.80	1.3	1	31.2	28.8	23.0	17.9	2.4	2.0	11.6	14.2	10.2	(76)	11.6
ZHEWEN INTERAT-A	600986 CH	CNY	5.82	1.2	115	35.6	27.9	19.1	14.9	0.4	0.4	10.6	15.5	12.0	(8)	10.6
BEIJING ZHIDEM-A	300785 CH	CNY	57.32	0.8	6	30.6	26.3	19.9	15.7	2.6	2.0	14.0	14.9	11.7	(71)	14.0
FOCUS TECH-A	002315 CH	CNY	16.57	0.8	12	21.5	-	17.3	-	3.2	-	-	10.6	-	(69)	-
SHENZHEN INFIN-A	002528 CH	CNY	3.79	0.7	6	-	-	-	-	-	-	-	-	-	30.0	-
				Average		26.0	23.8	19.1	15.6	2.6	2.1	12.9	13.6	13.5	11.1	(25)

Source: China Tonghai Securities estimates for Differ Group, Bloomberg consensus estimates for others
Note: HK- and China-listed shares priced as of 28 Feb 2022 close, others priced as of 27 Feb 2022

Key catalysts

1. **Faster-than-expected acquisitions of leading auto industry players:** The faster-than-expected acquisitions of auto industry-leading players will accelerate its market share expansion;

2. **Positive updates of key operating metrics in the O2O auto business:** The over-expected update in the auto e-commerce business, including revenue growth and car trading volume growth, will release a positive signal to the market in the business prospect and drive a rerating for Differ's shares;

3. **The incremental growth of China's auto consumer market:** The booming China's auto consumer market riding on the NEV replacement trends and the structural shift of auto consumer behavior to online will spawn ample opportunities for Cherries Car and catalyze its robust growth momentum.

Key risks

1. **Under-expected performance of automobile e-commerce business:** Slower-than-expected business expansion due to intensifying industry competition and lack of operation experience will cast a shadow on the market confidence in its new business;

2. **The failure to adapt to the rapid changes in the China auto value chain:** The rapid changes in the China auto value chain with increasing penetration of NEV may bring uncertainties to its O2O auto business;

3. **Fall in property value**: Differ Group is subject to the risk of property price depreciation as it holds a large amount of real estate investment assets.

DIFFER GROUP– COMPANY PROFILE

Company description

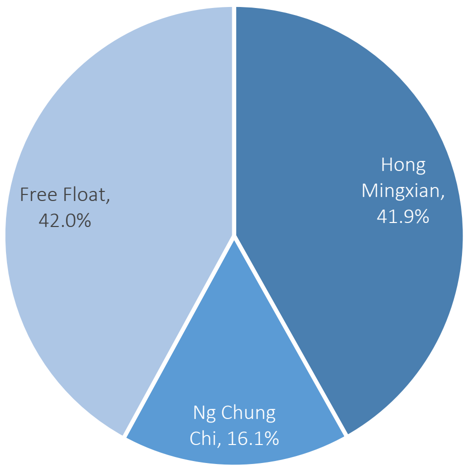
Established in 2008, Differ Group started as an integrated financing service provider, mainly providing short to medium-term financing for SMEs in China and engaging in asset management business with financial licenses. In 2021, it expanded the business into O2O auto platforms (branded as Cherries Car) to tap into the booming auto e-commerce market. In June 2015, it transferred to the main board from the GEM board of the HKEX.

Figure 26. Differ Group– Company milestone

Date	Event
Nov-2021	Announced the intent to acquire Sichuan Zhuzi Automobile
Sep-2021	Included in the FTSE China
Aug-2021	Acquired online auto e-commerce platform Qiancheng Taifeng Technology for RMB53mn and launched Cherries Car
May-2021	Launched automobile e-commerce business
Nov-2020	Included in the MSCI China Index
Sep-2019	Established strategic partnership with Wanda Group, Wyndham Hotel Group & CHINA Construction First Division Group
Jun-2018	Obtained licenses of Type 1 (Dealing in Securities) and Type 9 (Asset Management) from the HK SFC to carry out regulated activities
Nov-2016	Acquired the Differ Cultural Tourism Group
Jun-2015	Transferred to the main board of the HKEX (6878 HK)
Dec-2013	Listed on gem board of the HKEX (8056 HK)
Dec-2008	Differ Group was founded

Source: Company data

Figure 27. Differ Group– Shareholding structure



Source: HKEX

Note: As of 28 Feb 2022

Differ Group (6878 HK) Stock Rating: BUY

Income statement (RMB'mn)	2019	2020	2021E	2022E	2023E
Revenue	**2,306**	**6,170**	**1,786**	**4,162**	**5,154**
Cherries Car	0	0	7	1,621	2,486
Financial related services	145	185	193	196	199
Assets management business	778	709	820	2,154	2,383
Others	1,383	5,275	766	191	86
Cost of revenue	(1,867)	(5,628)	(1,089)	(1,917)	(2,235)
Gross profit	**438**	**542**	**697**	**2,246**	**3,775**
Operating expenses	0	0	(2)	(515)	(886)
Other income, net	(18)	(20)	(19)	(21)	(28)
EBIT	**420**	**522**	**675**	**1,710**	**2,861**
Finance costs	(43)	(89)	(145)	(180)	(179)
Other gain or loss, net	478	591	676	1,912	2,922
Pre-tax profit	435	503	531	1,732	2,743
Tax	(99)	(149)	(133)	(433)	(686)
Minority Interest	1	(3)	1	2	4
Attributable profits	**336**	**356**	**397**	**1,297**	**2,053**

Balance sheet (RMB'mn)	2019	2020	2021E	2022E	2023E
PPE	173	174	191	253	328
Investment properties	748	677	657	493	443
Other non-current assets	479	1,521	1,831	3,386	5,445
Inventories of properties	3,065	3,191	3,128	2,593	2,334
Finance lease, loan and account receivables	966	1,449	1,469	1,497	1,526
Cash and equivalents	140	88	403	314	485
Other current assets	367	1,048	850	909	837
Total assets	**5,938**	**8,148**	**8,529**	**9,445**	**11,397**
Long-term Borrowings	938	633	850	852	792
Other non-current liabilities	217	115	115	115	115
Accounts and bills payable	494	563	681	479	559
Short-term borrowings	545	389	400	350	320
Other current liabilities	2,153	4,099	3,737	2,646	2,551
Total liabilities	**4,347**	**5,800**	**5,783**	**4,442**	**4,337**
Total shareholders' Equity	1,587	2,306	2,703	4,957	7,011
Minority interests	4	42	43	45	49
Total equity	**1,591**	**2,348**	**2,746**	**5,003**	**7,060**

Cash flow statement (RMB'mn)	2019	2020	2021E	2022E	2023E
EBITDA	262	348	550	1,753	2,771
Other gains, net	13	24	125	152	151
Change in working capital	7	(732)	(242)	(791)	(1,159)
Tax Paid	(39)	(60)	(133)	(433)	(686)
Operating cash flow	**243**	**(420)**	**300**	**682**	**1,077**
Capex	(136)	(21)	(36)	(83)	(103)
Others	(295)	(344)	(33)	(1,416)	(534)
Investing cash flow	**(431)**	**(365)**	**(68)**	**(1,499)**	**(637)**
Change in borrowings	225	35	228	(48)	(90)
Interest paid	(54)	(118)	(149)	(181)	(176)
Others	68	821	5	958	(4)
Financing cash flow	**239**	**738**	**83**	**729**	**(269)**
Net change in cash	52	(47)	315	(89)	171
Free cash flow	**107**	**(441)**	**264**	**598**	**974**

Per Share Items (HKD)	2019	2020	2021E	2022E	2023E
Adjusted diluted EPS	0.06	0.06	0.07	0.22	0.35
DPS	0.00	0.00	0.00	0.00	0.00
BVPS	0.31	0.42	0.46	0.85	1.19

Ratio Analysis	2019	2020	2021E	2022E	2023E
Growth (YoY%)					
Revenue	161.9%	167.6%	(71.1%)	133.1%	23.8%
Gross profit	(3.6%)	15.7%	16.6%	400.3%	38.6%
Attributable profit	15.5%	6.1%	11.6%	226.4%	58.3%
Diluted EPS	(12.4%)	(1.7%)	5.4%	226.4%	58.3%
Margins					
Gross profit margin	19.0%	8.8%	39.0%	54.0%	73.2%
EBIT margin	18.2%	8.5%	37.8%	41.1%	55.5%
Attri. net profit margin	14.6%	5.8%	22.3%	31.2%	39.8%
Other ratios					
Return on assets	5.7%	4.4%	4.7%	13.7%	18.0%
Return on equity	21.1%	15.2%	14.5%	25.9%	29.1%
ROIC	10.9%	10.6%	9.9%	20.9%	25.1%
Dividend payout ratio	0.0%	0.0%	0.0%	0.0%	0.0%
Net debt to equity	84.4%	39.8%	30.8%	17.7%	8.9%
Interest coverage (X)	9.7	5.9	4.7	9.5	15.9
Valuation measures ratios					
PER (X)	37.1	37.8	35.8	11.0	6.9
PBR (x)	7.8	5.7	5.2	2.8	2.0
FCF yield (%)	0.7%	(2.7%)	1.5%	3.4%	5.6%
Dividend yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%

Key Operating Metrics	2019	2020	2021E	2022E	2023E
Revenue mix (%)					
Cherries Car	0.0%	0.0%	0.4%	38.9%	48.2%
Financial related services	6.3%	3.0%	10.8%	4.7%	3.9%
Assets management business	33.7%	11.5%	45.9%	51.8%	46.2%
Others	60.0%	85.5%	42.9%	4.6%	1.7%
Segment Growth (%)					
Cherries Car	N/A	N/A	N/A	24119%	53.4%
Financial related services	11.7%	28.0%	4.1%	1.7%	1.7%
Assets management business	8.8%	(8.8%)	15.7%	162.6%	10.6%
Others	3760.5%	281.4%	(85.5%)	(75.0%)	(55.0%)
Net profit mix of Cherries Car (%)					
Wholesale B2B business	N/A	N/A	14.8%	11.6%	11.7%
Auto financing solutions	N/A	N/A	46.3%	28.9%	17.7%
Retail B2C business	N/A	N/A	25.0%	12.6%	5.5%
Car marketplaces	N/A	N/A	12.5%	44.6%	62.1%
After-sale services	N/A	N/A	1.3%	2.3%	3.0%

Source: Company data, China Tonghai estimates
Note: FY End Dec

Rating Definitions	Disclaimer and Risk Statement
BUY We expect the stock to have a total return of > 10% over the next 12 months **HOLD** We expect the stock to have a total return of < 10% and >-10% over the next 12 months **SELL** We expect the stock to have a total return of < -10% over the next 12 months	This document is published by China Tonghai Securities Limited ("Tonghai Securities"), a licensed corporation (central entity number AAC577) regulated by the Securities and Futures Commission in Hong Kong. This document is for distribution in Hong Kong only to persons who are "Professional Investors" as defined in Part 1 of Schedule 1 of Securities and Futures Ordinance (Cap 571) of Hong Kong and any rules made thereunder. This document is not intended for distribution to or use by, any person or entity who is a citizen or resident of any jurisdiction where such distribution or use would be contrary to applicable law or regulation within such jurisdiction. This document does not constitute an offer or a solicitation of an offer to buy or sell any securities. This document is circulated to addresses solely and may not be reproduced or redistributed to any other person or published, in whole or in part, for any purpose. Tonghai Securities has not been in an investment banking relationship with the issuer within the preceding 12 months from the date of publication of this document. The research is based on information obtained from sources believed to be reliable, but Tonghai Securities does not make any representation or warranty as to its accuracy, completeness or correctness. Opinions expressed are subject to change without prior notice. Any recommendation does not have regard to specific investment objectives, financial situation and particular needs of any specific addressee. Tonghai Securities accepts no liability whatsoever for any direct or consequential loss arising from any use of this document. Tonghai Securities and its affiliates as well as persons associated with any of them from time to time may or may not have interests in the securities mentioned in this document. The prices of securities may move up or down, and past performance is not an indication of future performance. Investors shall consider seeking separate legal or financial advice before making investment decisions.
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