

China Yuchai International Limited
 NYSE: CYD

Maintaining Rating & Reducing Target
BUY, \$17.00
February 25, 2022
MARKET DATA

Share Price:	\$	11.83
Market Cap:	\$	483.26 M
52wk Range:	\$	10.57 - 19.59
Ave. Volume:		39,000
Basic S/O:		40.85 M
Fully Diluted S/O:		41.42 M
Float:		11.96 M
Institutional %:		26%
Insider %:		62%

FINANCIAL DATA (mrq)

Cash:	RMB	5,331.56 M
ST Debt:	RMB	N/A
Total Debt:	RMB	2,203.00 M
Book Value:	RMB	8,859.15 M
EBITDA (ttm):	RMB	1,133.19 M
FFO (ttm):	RMB	N/A

Auditor: Ernst & Young

	2020A	2021A	2022e	2023e
Revenue (in Millions of RMB)				
Jun	9,958.95	12,629.13	8,738.33	10,229.02
Dec	10,622.22	8,636.80	9,157.58	8,968.44
REV	20,581.17	21,265.93	17,895.92	19,197.46
<i>P/S</i>	<i>0.15</i>	<i>0.14</i>	<i>0.17</i>	<i>0.16</i>

Diluted EPS (in RMB)

Jun	7.48	6.21	4.17	7.07
Dec	5.95	0.46	3.98	4.64
EPS	13.43	6.67	8.15	11.71
<i>P/E</i>	<i>5.57</i>	<i>11.21</i>	<i>9.18</i>	<i>6.39</i>

Dividend (in USD)

DIV	1.70	0.30	0.40	0.50
<i>Yield</i>	<i>14.4%</i>	<i>2.5%</i>	<i>3.4%</i>	<i>4.2%</i>

 William Gregozeski, CFA
 wgregozeski@greenridgeglobal.com
 +1 414 435 1110

Sales & Gross Margins Better Than Expected In H2:21

Sales & Gross Margins Better Than Expected In H2:21. CYD reported H2:21 results yesterday with Revenue of RMB 8,636.8 million, an 18.7% decline from the year ago period. Unit sales declined 21.0%, to 171,449. The declines were better than the Commercial market as a whole, which saw sales down over 30% for the period. A bright spot for Yuchai was that all segments, outside of trucks, saw growth in the period, highlighted by continued demand for marine & power generation thanks in part to the recent power availability issues. Gross margins surged from the first half, to 15.4% and should continue to rise thanks to economies of scale from the National VI platform, per management on the conference call. Operating and Net Income ultimately fell below our estimate due to much heavier R&D spending than we expected. Management noted on the call that total R&D spending will likely stay just over RMB 1 billion each of the next two years. Net Income for the period was RMB 18.97 million, or RMB 0.46 per share.

Model Update. We made adjustments to our unit sales and Revenue estimates for 2022, which given current domestic economic uncertainties could result in a weaker than previously expected first half for the Commercial segment. We do expect sales to build through the pre-buy for National VIb implementation on July 1, 2023, and then fall off the next period as is typical. Gross margins should continue to rise as the Company works to cut costs and sees greater economies of scale on the National VI engine platform. The biggest adjustment to the model was a sharp increase in R&D spending, as it now appears the Company will spend RMB 1 billion (expensed and capitalized) per year going forward as it introduces new engine models and continues development of its New Energy platforms, including the recently announced Hydrogen engine.

Maintaining Rating & Reducing Target. The growth in non-Truck segments of the markets in the second half was a surprise, but the uncertainty with the property market and local/global economies provide near term uncertainty for sales. The Company is also investing heavily in its New Energy platforms and the timing of bringing products to market is unknown at this time, but offers optimism for future growth. With the estimate reductions we are reducing our target price from \$23.00 to \$17.00, but maintaining our Buy rating based on valuation. Our target price is based on the average of a P/E multiple of roughly 10 times our 2022 diluted EPS estimate of RMB 8.15 and an EV/EBITDA multiple of roughly 5 times our 2022 EBITDA estimate of RMB 1,085.4 million.

RISKS

Government Incentives & Policies

Sales in the commercial vehicle sector in China are dependent in part on the policies put in place by the Chinese government, which range from overall economic growth policies to national emissions standards to anti-overloading policies, among others.

New Energy Vehicles

The rise of new energy vehicles, and the incentives tied to them in China, have caused diesel engine sales to the bus market to fall in recent years, a trend we expect will continue. Additionally, movement from other vehicles traditionally powered by diesel engines, like construction vehicles, to electric will have a negative impact on CYD.

Financial Reporting & Auditing

Due to an accounting error the Company had to restate its 2005 financials. Since then CYD has not had any accounting irregularities, and has not had any material weaknesses in internal control since 2011.

Potential Delisting of Chinese Companies From US Exchanges

Recent legislation has surrounded the potential to bar Chinese companies from listing or raising money in the United States without a PCAOB audit, which China does not currently allow. It is unclear how this could impact CYD as it is Bermuda-based and controlled and managed by HLA in Singapore.

Staying Ahead of Emissions Standards

As a market leader, GYMCL must continue to invest in R&D and technological equipment to keep its engines ahead of the National emissions standards, which could come at increased costs to the Company. National VIa for diesel engines went into effect on July 1, 2021, with National VIb going into effect July 1, 2023.

No Formal Dividend Policy

CYD does not have a formal dividend policy and there are no assurances the Board will approve a dividend as predicted in our model.

Influence of HLA

HLA owns 44.0% of the shares of CYD and the Special Share, which gives it control over GYMCL. There are no assurances HLA will always act in the best interest of CYD shareholders. Similarly, should HLA sell off shares to lose the Special Share it is uncertain who would have control of GYMCL.

Heavy Management Turnover

While there has been stability in recent years, in the decade prior, the Company had undergone numerous changes to the positions of President, CFO and Board of Directors.

Past Disagreements with Yulin City Government

In 2003, CYD and HLA had severe disagreements over the status of GYMCL that led to a number of legal and operational issues, as well as a plan by HLA to diversify CYD away from diesel engines. While all parties have been on friendly terms since then, another such dispute could potentially arise at some point in the future.

Dependence on Dongfeng Group

Dongfeng Group, a long standing key customer and engine manufacturer, accounted for 29.2% of total Revenue in 2020, roughly flat from the year ago period when it accounted for 28.9% of total Revenue, an absolute increase in Revenue of roughly RMB 800,000,000. Sales to Dongfeng, and other customers in China, could fall in 2021 due to the impact of COVID-19 and related supply chain issues. The loss of Dongfeng would have a substantial adverse impact on future results.

ESTIMATED INCOME STATEMENT

	2020A	H1:21A	H2:21A	2021e	H1:22e	H2:22e	2022e	H1:23e	H2:23e	2023e
<i>Total Units Sold</i>	430,320	285,342	171,449	456,791	183,844	196,429	395,526	274,972	185,426	427,050
Revenue	20,581,170	12,629,126	8,636,804	21,265,930	8,738,334	9,157,581	17,895,915	10,229,015	8,968,444	19,197,459
Cost of Sales	(17,391,599)	(11,005,305)	(7,308,512)	(18,313,817)	(7,368,059)	(7,717,839)	(15,085,897)	(8,522,654)	(7,522,752)	(16,045,406)
Gross Profit	3,189,571	1,623,821	1,328,292	2,952,113	1,370,276	1,439,742	2,810,018	1,706,361	1,445,692	3,152,053
Other Operating Income	378,947	111,702	204,487	316,189	106,973	109,653	216,626	112,407	115,240	227,647
Research & Development	(626,478)	(315,696)	(533,116)	(848,812)	(349,533)	(366,303)	(715,837)	(409,161)	(358,738)	(767,898)
SG&A	(1,760,036)	(920,058)	(835,899)	(1,755,957)	(786,450)	(860,813)	(1,647,263)	(869,466)	(843,034)	(1,712,500)
Operating Income	1,182,004	499,769	163,764	663,533	341,266	322,279	663,545	540,142	359,160	899,302
Finance Costs	(151,170)	(68,410)	(47,518)	(115,928)	(62,916)	(59,934)	(122,850)	(57,104)	(54,418)	(111,522)
Share of Associates & JVs	(58,970)	12,482	(108,377)	(95,895)	1,223	4,079	5,302	(3,464)	6,448	2,984
Profit Before Tax	971,864	443,841	7,869	451,710	279,573	266,425	545,997	479,574	311,190	790,764
Income Tax Expense	(192,538)	(86,251)	42,435	(43,816)	(55,915)	(53,285)	(109,199)	(95,915)	(62,238)	(158,153)
Net Profit	779,326	357,590	50,304	407,894	223,658	213,140	436,798	383,659	248,952	632,611
Non-Controlling Interests	(230,424)	(103,883)	(31,338)	(135,221)	(58,151)	(55,416)	(113,567)	(99,751)	(64,728)	(164,479)
Net Profit to Shareholders	548,902	253,707	18,966	272,673	165,507	157,723	323,230	283,908	184,224	468,132
Basic EPS	13.43	6.21	0.46	6.67	4.05	3.86	7.91	6.95	4.51	11.46
Basic S/O	40,858	40,858	40,858	40,858	40,858	40,858	40,858	40,858	40,858	40,858
Diluted EPS	13.43	6.21	0.46	6.67	4.05	3.86	7.91	6.95	4.51	11.46
Diluted S/O	40,858	40,858	40,858	40,858	40,858	40,858	40,858	40,858	40,858	40,858
Dividend (in USD)	\$ 1.70			\$ 0.30			\$ 0.30			\$ 0.50
Gross Profit	15.5%	12.9%	15.4%	13.9%	15.7%	15.7%	15.7%	16.7%	16.1%	16.4%
Operating Income	5.7%	4.0%	1.9%	3.1%	3.9%	3.5%	3.7%	5.3%	4.0%	4.7%
Net Margin	2.7%	2.0%	0.2%	1.3%	1.9%	1.7%	1.8%	2.8%	2.1%	2.4%

Source: CYD documents filed with the SEC and Greenridge Global estimates

DISCLOSURES**Distribution of Ratings**

Rating	Count	Percent	<u>I.B. last 12 months</u>	
			Count	Percent
BUY	9	100%	0	0%
HOLD	0	0%	0	0%
SELL	0	0%	0	0%
NO RATING	0	0%	0	0%

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- BUY:** Describes undervalued stocks we expect to provide a total return (capital appreciation + yield) of 15% or more in the next twelve month period.
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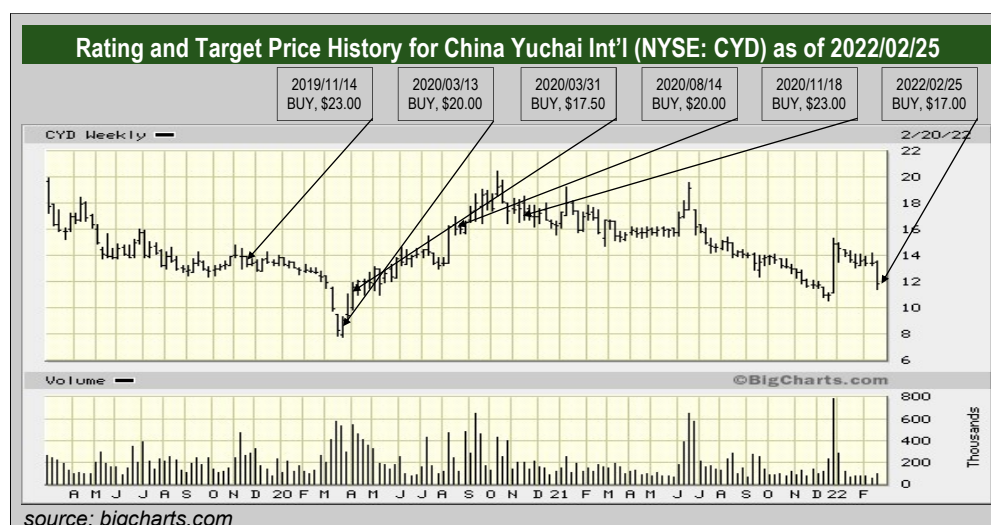
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<u>Company</u>	<u>Disclosures</u>
China Yuchai International Limited	-

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William Gregozeski, CFA
+1 414 435 1110
wgregozeski@greenridgeglobal.com

Greenridge Global LLC
10 S. Riverside Plaza
Suite 875
Chicago, IL 60606 USA
www.greenridgeglobal.com