



August 29, 2014
Company Report
Rating: HOLD
TP: HK\$ 4.80

H-Share price (HK\$)	5.17
Est. share price return	(7.16%)
Est. dividend yield	1.39%
Est. total return	(5.77%)

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Key Data

52Wk H/L(HK\$)	6.80 / 3.92
Issued shares (mn)	996
H-Shares (mn)	402
A-Shares (mn)	594
Market cap	
H-shares (HK\$ mn)	2,078
A-Shares (mn) (RMB mn)	4,805
3-mth avg daily turnover (HK\$ mn)	20.5
Major shareholder(s) (%):	
SINOMACH (SOE)	74.74

Source(s): Company, Bloomberg, ABCI Securities

1H14 Revenue breakdowns (%)

Agricultural Machinery	83.19
Power Machinery	14.94
Financial Leasing Income	0.68
Others	1.19

Source(s): Company, ABCI Securities

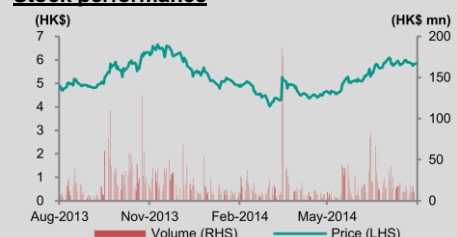
Share performance (%)

	Absolute	Relative*
1-mth	(2.86)	(6.18)
3-mth	25.65	15.66
6-mth	18.69	5.63

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

Stock performance



Source(s): Bloomberg, ABCI Securities

First Tractor (38 HK)
2H sales unlikely to recover; More provision loss expected; Downgrade to HOLD

- Revenue dropped 17.5% YoY and net income dropped 39.8% YoY in 1H14 due to the sluggish tractor sales
- GPM increased 2.4ppt YoY to 17.3% in 1H14 under changes in sales arrangement and effective cost control
- Provision loss increased ~90% YoY to RMB 72mn in 1H14. We expect 2H provision to be RMB 100mn amid poor liquidity in the machinery market
- We revise down our FY14E/15E earnings forecasts and lower our TP to HK\$ 4.80 based on 20x of FY14E EPS. Downgrade to **HOLD**

Sluggish 1H14 results. Revenue dropped 17.5% YoY to RMB 5,474mn and net income dropped 39.8% YoY to RMB 112mn in 1H14. The decline in sales was mainly due to the lukewarm agricultural machinery procurement during 1H14. Sales volume of mid-to-high powered tractor in First Tractor dropped 18.3% YoY in 1H14, in line with the overall market decline of 17.2% YoY during the same period. Going forward, we expect the market would still be digesting the additional capacity in the mid-to-high powered tractor segment after the rapid expansion in 2009-13. Based on our discussion with management, we believe tractor sales in 2H14 is unlikely to recover.

GPM rises on changes in sales arrangement. GPM increased 2.4ppt YoY to 17.3% in 1H14 on changes in sales arrangement. The Group raised the selling price in 1H14 but bore the logistic cost of delivering from production base to distributors. Nevertheless, if reallocating the increased logistic cost to costs of sales, GPM improved by 1.1ppt YoY in 1H14, thanks to the deflated raw material costs and cost control.

Provision loss increased. The Group made a provision of RMB 72mn on receivables in 1H14 (vs. RMB 38mn in 1H13), offsetting the gains of higher margins resulting from improved cost control. Net margin dropped 0.8ppt YoY in 1H14. Under the sluggish business environment, we expect the Group to make another provision of ~RMB 100mn in 2H14, eradicating the positive effects on GPM improvement.

Downgrade to HOLD. Looking forward, we expect that demand for tractor would remain weak in 2H14. We lower our profit FY14E/15E forecasts due to the sluggish market situation and higher-than-expected provision in FY14. Nevertheless, the Group's H share is at a deep discount (~50%) to its A shares. With the Shanghai-HK mutual stock market access scheme expecting to commence soon, we believe this price differential may offer some push to the share price in the near term. Our new TP of HK\$ 4.80 represents 20x FY14E P/E, equivalent to the upper quartile of its historical P/E since 2011.

Risk factors: 1) Provisional loss increase amid poor business environment; 2) Newcomers stiffens market competition; 3) Delay, changes or cancellation of the Shanghai-HK mutual stock market access scheme.

Results and Valuation

FY ended Dec 31	2012A	2013A	2014E	2015E	2016E
Revenue (RMB mn)	11,508	11,038	9,606	10,181	10,761
Chg (% YoY)	(1.67)	(4.08)	(12.97)	5.98	5.70
Net Income (RMB mn)	325	222	191	233	293
Chg (% YoY)	(26.14)	(31.69)	(13.93)	22.10	25.77
EPS (RMB)	0.363	0.223	0.192	0.234	0.295
P/E (x)	-	18.63	21.65	17.73	14.10
BVPS (RMB)	4.930	4.492	4.815	5.267	5.790
P/B (x)	-	0.92	0.86	0.79	0.72
DPS (RMB)	0.111	0.067	0.058	0.070	0.088
Yield (%)	-	1.61	1.39	1.69	2.13
ROAE (%)	8.30	4.99	4.12	4.65	5.33
Net gearing (%)	Net Cash	5.66	16.45	9.20	Net Cash

* Net gearing=Net debt/Total equity

Source(s): Bloomberg, ABCI Securities estimates

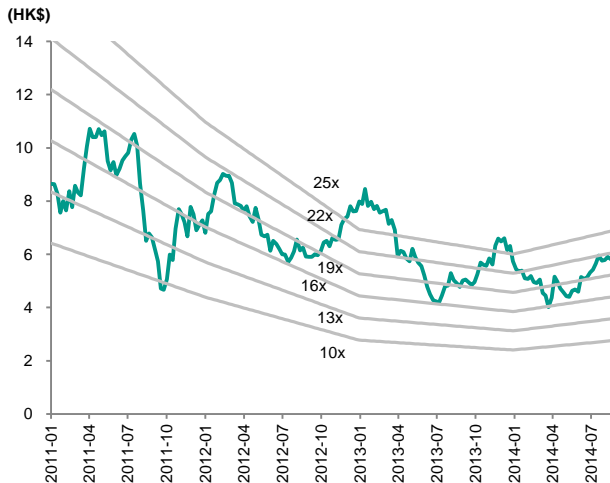


Exhibit 1: Financial summary of First Tractor in 1H12-1H14

	1H12	2H12	1H13	2H13	1H14	(% YoY)
Revenue (RMB mn)	6,691	4,817	6,634	4,404	5,474	(17.49)
Agricultural Machinery	5,597	4,215	5,658	3,725	4,554	(19.51)
Power Machinery	734	490	851	613	818	(3.88)
Financial Leasing Income	46	41	33	40	37	12.12
Others	314	71	92	26	65	(29.35)
Less: Operating cost (RMB mn)	5,759	4,197	5,648	3,685	4,528	(19.83)
Gross Profit (RMB mn)	932	620	986	719	946	(4.06)
GPM (%)	13.93	12.87	14.86	16.33	17.28	2.42ppt
SG&A (RMB mn)	574	547	682	567	741	8.65
Selling and distribution cost	194	161	229	175	260	13.54
Administrative cost	380	386	453	392	481	6.18
SG&A-to-revenue (%)	8.58	11.36	10.28	12.87	13.54	3.26ppt
Net profit (RMB mn)	261	64	186	36	112	(39.78)
Net profit margin (%)	3.90	1.33	2.80	0.82	2.05	(0.76ppt)
Total receivables assets (RMB mn)	3,733	3,129	4,106	3,047	3,391	
Trade and bill receivables	2,950	2,335	3,298	2,322	2,456	
Financial leasing assets	783	794	808	725	935	
As percentage of revenue (%)	55.79	64.96	61.91	69.16	61.95	0.04ppt
Total debt (RMB mn)	1,288	1,069	2,050	2,176	2,604	
Total cash and equivalents (RMB mn)	1,378	1,968	1,702	1,880	1,449	
Net debt (Net cash) (RMB mn)	(90)	(899)	348	296	1,155	231.90
Total equity (RMB mn)	4,083	4,942	5,152	5,228	5,264	
Net gearing (%)	Net Cash	Net Cash	6.75	5.66	21.94	15.19ppt

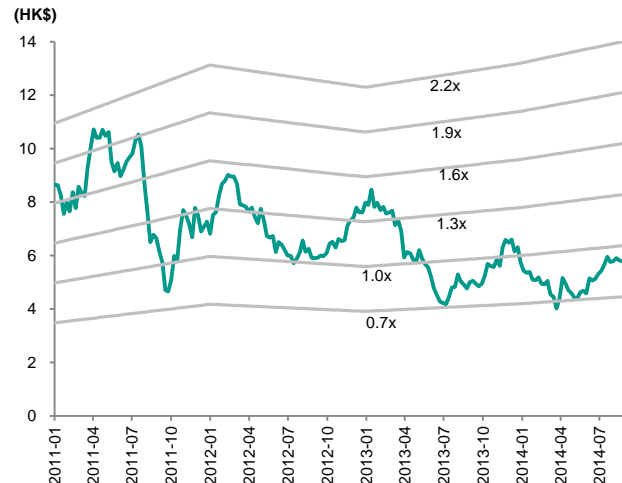
Source(s): Company, ABCI Securities

Exhibit 2: P/E band of First Tractor-H in 1M11-8M14



Source(s): Company, Bloomberg, ABCI Securities estimates

Exhibit 3: P/B band of First Tractor-H in 1M11-8M14



Source(s): Company, Bloomberg, ABCI Securities estimates

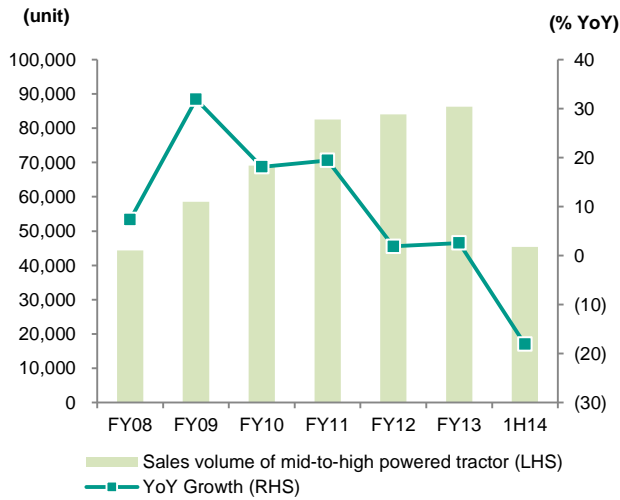
Exhibit 4: Valuation of domestic and international agricultural machinery manufacturers

Company	Ticker	Mkt cap		As of 28/8/2014		P/E (x)		EPS (%YoY)		P/B (x)		ROAE (%)	
		(HK\$ mn)	CRY	Share Price	FY14E	FY15E	FY14E	FY15E	FY14E	FY15E	FY14E	FY15E	
DEERE & CO	DE US	236,409	USD	83.85	10.02	12.24	(8.81)	(18.17)	2.75	2.52	27.86	19.64	
MAHINDRA & MAHIN	MM IN	110,794	INR	1,407.2	17.26	13.45	3.14	28.32	3.27	2.84	17.92	15.98	
FIRST TRACTOR-H	38 HK	2,078	HKD	5.17	21.65	17.73	(13.93)	22.10	0.86	0.79	4.12	4.65	
FIRST TRACTOR-A	601038 CH	6,061	CNY	8.09	44.94	40.45	(13.93)	22.10	1.59	1.54	4.12	4.65	
ESCORTS LTD	ESC IN	1,784	INR	113.85	8.30	6.31	(33.48)	31.45	0.66	0.61	8.44	10.04	
DEERE & CO	DE US				12.91	13.12	(5.42)	(2.92)	2.87	2.58	24.13	18.10	
Sector Weighted Average		236,409	USD	83.85	10.02	12.24	(8.81)	(18.17)	2.75	2.52	27.86	19.64	

Source(s): Bloomberg, ABCI Securities estimates

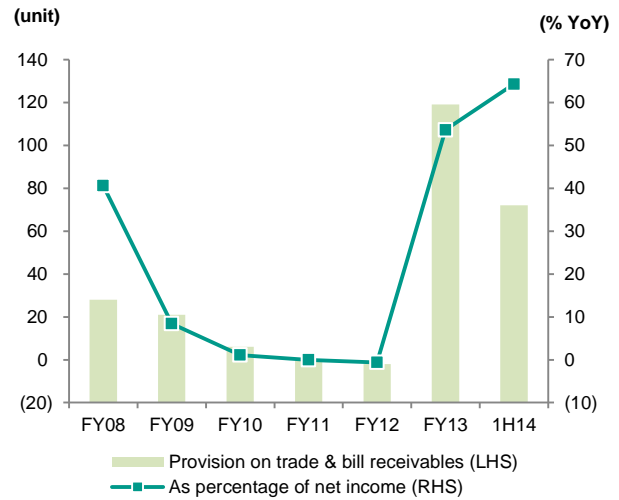


Exhibit 5: Sales volume of mid-to-high powered tractor by the Group and the growth, FY08-1H14



Source(s): Company, ABCI Securities

Exhibit 6: Provision on trade & bill receivables and as percentage of net income, FY08-1H14



Source(s): Company, ABCI Securities

Exhibit 7: FY14E-15E financial projections for First Tractor

	FY14E			FY15E		
	Previous	New	Chg (%)	Previous	New	Chg (%)
Revenue (RMB mn)	12,666	9,606	(24.15)	14,960	10,181	(31.94)
Gross profit (RMB mn)	1,803	1,657	(8.07)	2,310	1,766	(23.55)
GPM (%)	14.23	17.25	3.02ppt	15.44	17.35	1.91ppt
Net income (RMB mn)	528	191	(63.79)	789	233	(70.45)
Net margin (%)	4.17	1.99	(2.18ppt)	5.28	2.29	(2.99ppt)
EPS (RMB)	0.530	0.192	(63.82)	0.793	0.234	(70.48)
BVPS (RMB)	5.154	4.815	(6.59)	5.998	5.267	(12.19)
DPS (RMB)	0.159	0.058	(63.82)	0.238	0.070	(70.48)

Source(s): ABCI Securities estimates



Financial statements of the Group

Consolidated income statement (2012A-2016E)

FY Ended Dec 31 (RMB mn)	FY12A	FY13A	FY14E	FY15E	FY16E
Revenue	11,508	11,038	9,606	10,181	10,761
Agricultural Machinery	9,812	9,383	7,820	8,314	8,810
Power Machinery	1,224	1,464	1,610	1,691	1,775
Financial Leasing Income	87	73	82	77	71
Others	385	118	94	99	104
COGS	(9,956)	(9,333)	(7,949)	(8,414)	(8,927)
Gross profit	1,552	1,705	1,657	1,766	1,834
SG&A	(1,121)	(1,249)	(1,165)	(1,237)	(1,309)
Other income and gains	30	(122)	(229)	(208)	(120)
Pre-tax profit	461	334	263	322	405
Income tax	(71)	(72)	(39)	(48)	(61)
Net profit	390	262	223	274	344
Profit attributable to:					
Minority interests	65	40	32	40	51
Equity shareholders of the Company	325	222	191	233	293
EPS (RMB)	0.363	0.223	0.192	0.234	0.295
DPS (RMB)	0.111	0.067	0.058	0.070	0.088
EBIT	545	419	354	412	493
EBITDA	765	668	627	689	775

Source(s): Company, ABCI Securities estimates

Consolidated balance sheet (2012A-2016E)

As of Dec 31 (RMB mn)	FY12A	FY13A	FY14E	FY15E	FY16E
Current assets	7,648	7,765	7,096	7,527	8,318
Cash and equivalent	1,968	1,880	1,140	1,449	2,037
Trade and bill receivables	2,335	2,322	2,415	2,494	2,518
Financial leasing receivables	748	710	628	624	541
Inventories	1,470	1,766	1,719	1,647	1,777
Other current assets	1,127	1,086	1,195	1,314	1,445
Non-current assets	3,690	4,296	4,478	4,564	4,649
Property, plant and equipment	2,559	3,098	3,253	3,304	3,352
Prepaid land lease payment	758	863	864	863	863
Intangible assets	64	65	66	68	68
Long-term investments	167	147	162	178	196
Other non-current assets	142	123	134	151	169
Total assets	11,338	12,060	11,574	12,091	12,967
Current liabilities	5,570	4,983	4,074	4,028	4,260
Trade and bill payables	2,703	2,747	1,826	1,862	1,806
Receipts in advance	1,047	569	584	434	642
Short term borrowings	451	592	481	431	381
Other current liabilities	1,369	1,075	1,183	1,301	1,431
Non-current liabilities	826	1,849	1,876	1,905	1,937
Long-term borrowings	618	1,584	1,584	1,584	1,584
Other non-current liabilities	208	265	292	321	353
Total liabilities	6,396	6,832	5,949	5,933	6,197
Minority interests	525	754	829	912	1,004
Shareholders' equities	4,417	4,474	4,796	5,246	5,767
BVPS (RMB)	4.930	4.492	4.815	5.267	5.790

Source(s): Company, ABCI Securities estimates



Consolidated cash flow statement (2012A-2016E)

FY ended Dec 31 (RMB mn)	FY12A	FY13A	FY14E	FY15E	FY16E
Profit before tax	461	334	263	322	405
Changes in depreciation and amortization	220	249	274	277	281
Changes in working capital	(91)	(760)	(641)	(398)	3
Financial cost	63	80	91	90	88
Income tax paid	(98)	(66)	(39)	(48)	(61)
Others	(63)	31	(0)	-	-
CF Operating	492	(132)	(53)	243	717
Increase in PP&E	(594)	(764)	(400)	(300)	(300)
Increase in intangible assets	(49)	(106)	(1)	(1)	(1)
Others	(145)	354	-	-	-
CF Investing	(788)	(516)	(401)	(301)	(301)
Capital injection	866	-	-	-	-
Net debt financing	(86)	1,107	(111)	(50)	(50)
Dividend payout	(76)	(76)	(67)	(57)	(70)
Interest paid	(83)	(83)	(91)	(90)	(88)
Others	35	(293)	(17)	565	381
CF Financing	656	655	(286)	368	173
Net change in cash	360	7	(740)	309	589
Cash at the beginning	1,541	1,968	1,880	1,140	1,449
Adjustment (Time deposit & FX effect)	67	(95)	-	-	-
Cash at the end	1,968	1,880	1,140	1,449	2,037

Source(s): Company, ABCI Securities estimates

Key operating and financial ratios (2012A-2016E)

FY ended Dec 31	FY12A	FY13A	FY14E	FY15E	FY16E
Sales mixed (%)					
Agricultural Machinery	85.26	85.01	81.40	81.66	81.87
Power Machinery	10.64	13.26	16.76	16.61	16.50
Financial Leasing Income	0.76	0.66	0.85	0.75	0.66
Others	3.35	1.07	0.98	0.97	0.97
Profit & loss ratios (%)					
Gross margin	13.49	15.45	17.25	17.35	17.04
Net profit margin	2.82	2.01	1.99	2.29	2.73
Effective tax rate	15.40	21.56	15.00	15.00	15.00
Growth (%)					
Revenue	(1.67)	(4.08)	(12.97)	5.98	5.70
Gross profit	(6.51)	9.86	(2.80)	6.58	3.84
EBIT	(17.67)	(23.12)	(15.54)	16.32	19.87
EBITDA	(4.61)	(12.68)	(6.07)	9.83	12.39
Net profit	(26.14)	(31.69)	(13.93)	22.10	25.77
Balance sheet ratios					
Current ratio (x)	1.37	1.56	1.74	1.87	1.95
Quick ratio (x)	1.11	1.20	1.32	1.46	1.54
Cash ratio (x)	0.35	0.38	0.28	0.36	0.48
Trade and bill receivables days	77	77	90	88	85
Trade and bill payables turnover days	93	107	105	80	75
Inventory turnover days	49	63	80	73	70
Total debt / equity ratio (%)	21.63	41.62	36.71	32.72	29.02
Net debt / equity ratio (%)	Net Cash	5.66	16.45	9.20	Net Cash
Returns (%)					
ROAE	8.30	4.99	4.12	4.65	5.33
ROAA	3.69	2.24	1.89	2.31	2.75
Payout ratio	30.64	30.00	30.00	30.00	30.00

Source(s): Company, ABCI Securities estimates



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Definition of equity rating

Rating	Definition
Buy	Stock return \geq Market return rate
Hold	Market return $- 6\% \leq$ Stock return $<$ Market return rate
Sell	Stock return $<$ Market return $- 6\%$

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate from 2007-2011

Time horizon of share price target: 12-month

Definition of share price risk

Rating	Definition
Very high	$2.6 \leq$ 180 day volatility/180 day benchmark index volatility
High	$1.5 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 2.6
Medium	$1.0 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 1.5
Low	180 day volatility/180 day benchmark index volatility $<$ 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index.

Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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