

Company Rating:
Buy
Target price: HK\$9.27

First Tractor (38 HK) Construction & Farm Machinery Industry

Enjoy Low Financing Cost for Expansion

Key data

H-share price (HK\$)	7.57
Upside potential (%)	22.4
52Wk H/L(HK\$)	9.20/5.43
Issued shares (mn)	996
H-share	402
A-share	594
H-share market cap (HK\$mn)	3,043
30-day avg daily vol (HK\$mn)	24.8
Auditors	Baker Tilly
Major shareholder (%)	
YTO Group	44.52

Source: Company & Bloomberg

Revenue breakdown by product (%)

Agricultural machinery	82.6
Power machinery	11.7
Other machinery	5.0
Financial operations	0.8

*Based on 1HFY12 results

Source: Company

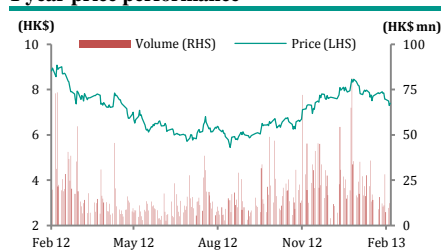
Share performance (%)

	Absolute	Relative ¹
1-mth	-4.1	-1.4
3-mth	3.6	-0.9
6-mth	25.1	6.2

1: Relative to Hang Seng Index

Source: Bloomberg

1 year price performance



Source: Bloomberg

Analyst Information

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Previous report
Date: February 26, 2013
Rating: Buy
Target price: HK\$9.27

High-power tractor maker First Tractor will issue Rmb800mn bond at coupon rate in range of 4.7-5.0%p.a. to repay its expensive bank loans which are charged at 6.0%. We estimate it will save Rmb6.0-7.8mn interest expenses. Under the favorable subsidy policies for development of agricultural machineries, we believe the Group will leverage on the low cost financing to support its expansion during 2013 to 2015. The counter is trading at 9.4x FY2013E PER, which is 18.3% discount to its 3-yr average PER of 11.5x. We reiterate "Buy" on First Tractor.

Issue Rmb800mn bond. In order to lower the financial cost, the Group plans to issue 5-year Rmb800mn bond at coupon rate of 4.7-5.0%. 75% of the net proceeds will be used to repay the bank loans with interest rate estimated at 6%. We estimate that the Group will save the financial cost by Rmb6.0-7.8mn in FY2013. The rest of the 25% net proceeds will be used to enlarge the working capital.

Good earning quality enjoys low interest rate. The operating cash flow of the Group is strong. The operating cash flow/Net income ratio of the Group was 63.2%, in average, during FY2009 to 1-3QFY2012, which is comparable to the global player Deere & Co (DE US) at 69.0%. We like the good earning quality of the Group so that it can enjoy low financing cost. The benchmark lending rate for 3-5Yr is 6.4% according to the PBOC.

Reiterate Buy. We believe that the Group will ambitiously expand the production capabilities for hi-powered tractors under the favorable subsidy programs in 2013-14. According to the Group, it is approved by CSRC to issue another Rmb700mn bond by 2014. Under the good sentiment of the Group, we believe that it can continue to enjoy the low cost financing to support the expansion and M&As in the future. We maintain "Buy" on First Tractor.

Risk factors: Product concentration risk; Development of agricultural machineries subject to policy risk; Raw material inflation risk

Forecast and Valuation

FY ended Dec 31	FY10A	FY11A	FY12E	FY13E	FY14E
Revenue (Rmb mn)	10,266	11,328	10,770	13,872	19,129
Chg (%YoY)	14.0	10.3	(4.9)	28.8	37.9
Net Income (Rmb mn)	543	411	402	645	971
Chg (%YoY)	118.3	(24.3)	(2.3)	60.7	50.6
EPS (Rmb)	0.642	0.486	0.436	0.648	0.975
Chg (%YoY)	118.3	(24.3)	(10.2)	48.6	50.6
PER (x)	-	12.67	13.95	9.39	6.23
PBR (x)	-	1.60	1.32	1.34	1.23
Yield (%)	-	-	2.15	3.20	4.81
ROAA (%)	7.3	4.5	3.9	5.2	6.6
ROAE (%)	16.4	11.2	9.3	13.0	18.2
Net debt/total equity (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company, ABCI Securities estimates

Financial highlights of the Group

	1H11	1-3Q11	FY11	1H12	1-3Q12	1H12 (% YoY)	1-3Q12 (% YoY)
Revenue (Rmb mn)	7,165	9,536	11,328	6,304	9,104	-12.02	-4.53
Agricultural machineries	5,999		9,356	5,208	7,546 ¹	-13.19	
Power machineries	866		1,470	735	1,091 ¹	-15.13	
Other machineries	274		436	313	395 ¹	14.17	
Financial operations	26		66	48	72 ¹	83.88	
Gross Profit	913	1,277	1,559	884	1,267	-3.18	-0.78
Agricultural machineries	692		1,058	624		-9.85	
Power machineries	157		409	168		6.86	
Other machineries	39		32	48		22.10	
Financial operations	24		60	44		83.88	
GPM (%)	12.74	13.39	13.76	14.02	13.92	1.28ppts	-13.39ppts
Agricultural machineries	11.54		11.30	11.98		0.44ppts	
Power machineries	18.15		27.80	22.85		4.70ppts	
Other machineries	14.40		7.45	15.40		1.00ppts	
Financial operations	90.00		91.31	90.00		0.00ppts	
Major cost (Rmb mn)							
Selling cost	(227)	(302)	(360)	(190)	(277)	-16.30	-8.28
Administrative cost	(343)	(538)	(677)	(351)	(548)	2.33	1.86
Finance cost	(28)	(40)	(45)	(36)	(55)	28.57	37.50
Cost ratio (%)							
Selling cost	3.17	3.17	3.18	3.01	3.04	-0.15ppts	-0.12ppts
Administrative cost	4.79	5.64	5.98	5.57	6.02	0.78ppts	0.38ppts
Finance cost	0.39	0.42	0.40	0.57	0.60	0.18ppts	0.18ppts
Net profit (Rmb mn)	271	317	411	286	326	5.54	2.84
Net profit margin (%)	3.78	3.32	3.63	4.54	3.58	0.75ppts	0.26ppts
Operating cash flow (Rmb mn)	(143)	77	635	4	(498)	-102.80	-746.75
OCF/Net income (%)	-52.77	24.29	154.57	1.40	-152.76	54.17ppts	-177.05ppts

1: Estimated by ABCI Securities

Source: Company

Consolidated income statements forecast

FY ended Dec 31 (Rmb mn)	FY10A	FY11A	FY12E	FY13E	FY14E
Revenue	10,266	11,328	10,770	13,872	19,129
Agricultural machineries	8,141	9,356	9,006	11,430	16,321
Power machineries	1,225	1,470	1,194	1,708	1,844
Other machineries	855	436	480	603	751
Financial operations	45	66	90	131	213
Cost of sales	(8,749)	(9,769)	(9,290)	(11,721)	(16,132)
Gross profit	1,517	1,559	1,480	2,151	2,997
Other income and gains	170	68	62	62	63
Selling and distribution	(368)	(360)	(326)	(432)	(565)
Administrative expenses	(646)	(677)	(677)	(944)	(1,278)
EBIT	673	590	539	838	1,217
Finance costs	(28)	(54)	(42)	(57)	(56)
Associates	1	-	-	-	-
Pre-tax profit	646	536	497	781	1,161
Profits tax	(84)	(79)	(70)	(109)	(163)
Minority interests	(20)	(47)	(26)	(27)	(28)
Net profit	543	411	402	645	971

Source: Company, ABCI Securities estimates

Peer group valuation and earnings forecasts summary of agricultural machinery sectors

Company	Ticker	MKT CAP ¹ (HKD mn)	Share Price	PER (x)		EPS Change (%)		PBR (x)		ROAE (%)	
				FY2012	FY2013	FY2012	FY2013	FY2012	FY2013	FY2012	FY2013
Agricultural Machinery Makers											
DEERE & CO	DE US	264,206	USD 87.82	10.24	9.73	11.06	5.27	3.55	2.86	38.74	39.34
MAHINDRA & MAHIN	MM IN	77,461	INR 880.50	13.88	11.41	19.25	21.67	2.59	2.21	21.10	20.14
CNH GLOBAL NV	CNH US	82,444	USD 44.34	9.14	8.64	3.68	5.79	1.08	0.96	11.99	12.79
FIRST TRACTOR-H ²	38 HK	3,043	HKD 7.57	13.95	9.39	-10.22	48.58	1.32	1.34	9.30	13.00
FIRST TRACTOR-A ²	601038 CH	7,745	RMB 10.45	23.97	16.13	-10.22	48.58	2.27	2.30	9.30	13.00
ESCORTS LTD	ESC IN	1,093	INR 62.25	6.94	5.09	44.88	36.44	0.40	0.40	6.43	7.21
Sector Weighted Average				10.94	9.92	10.68	9.43	2.86	2.36	29.74	30.18

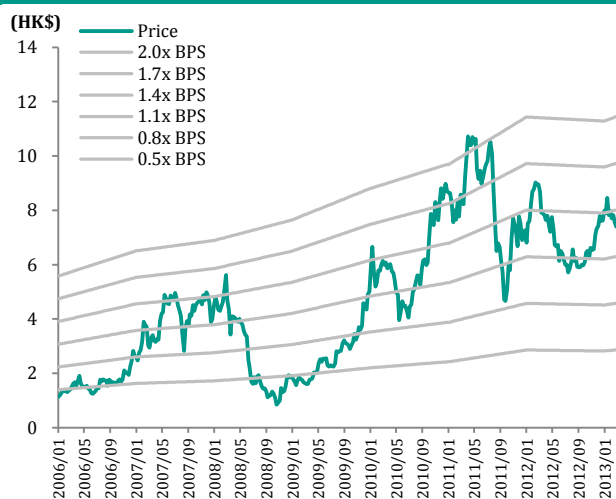
* The data in the table is as at February 28, 2013;

1: The market capital value of the companies are translated into HKD;

2: ABCI Securities estimates;

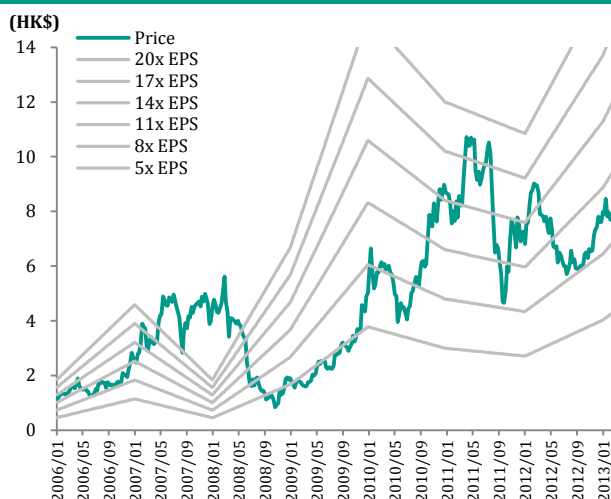
Source: Bloomberg, ABCI Securities estimates

PB band of the Group



Source: Company, Bloomberg, ABCI Securities estimates

PE band of the Group



Source: Company, Bloomberg, ABCI Securities estimates

Disclosures

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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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