

# Renault SA

## Strong organic growth and margin expansion – Buy

### Best-in-class organic growth should support margin expansion

We continue to like Renault on a combination of (1) strong organic growth ahead, (2) margin expansion potential and (3) EM optionality, and we stand 5-10% above consensus EPS. Organic growth drivers: Busy product renewal over the next 12-18 months (30%-plus of product portfolio renewed), which is mainly covering higher segments (C/D). The contribution from "sales to partners" (Daimler/Nissan) should stay at high levels (c50% of revenue growth so far this year). Margin expansion drivers: New launches should support product mix/pricing and are produced on the CMF modular platform (from 5% of total production this year to 20% next year, reaching 50%-plus by 2020E). "Sales to partners" should continue to boost the utilisation rate in Europe.

### Seeing the light at the end of the tunnel in emerging markets medium term?

While we think it is too early to turn bullish on emerging markets, data in our [Evidence Lab report](#) suggests that Renault is investing in the right segment (SUV) and locations (tier 2 and 3 cities) in China. Leveraging Nissan's past experience with the "copy and paste" strategy should allow the JV to rapidly deliver double-digit margins (we assume 10-15%). All in all, the direct earnings contribution of China is likely to remain below c5% of the group (c15%, including Nissan). Looking at other emerging markets, we note: (1) Renault delivery has been impressive in markets that have turned much worse than expected; and (2) the risk is currently skewed to the upside. Assuming Brazil and Russia return to each weighing about 8-9% of Renault's unit sales, operations resume in Iran and China is off to a strong start, we quantify an incremental EPS contribution of about €1.5 in 2016E (c10% impact versus UBS base case), all else remaining equal.

### Surfing on the "low-cost" wave for longer

Renault recently launched its low-cost model in India (Kwid) and orders are already running above production capacity. We believe Renault should continue to surf on the low-cost wave for longer without meaningful competition for another few years (VW emissions scandal and end of Suzuki partnership could delay plans).

### Valuation: Buy, €110 PT (was €95; DCF for core + DDM mid-point for associates)

Renault trades on EV/sales of 0.07x, 0.8x EBITDA and PE of 7.1x (2016E). Applying a 20% discount to equity stakes yields 0.15x, 1.9x and 3.7x, respectively. We raise our estimates to reflect the Evidence Lab data from China, a stronger Q3 and a higher contribution from Nissan.

### Equities

France  
Automobile Manufacturers

12-month rating **Buy**

12m price target **€110.00**  
Prior: **€95.00**

Price **€92.57**

RIC: RENA.PA BBG: RNO FP

### Trading data and key metrics

52-wk range €98.81-57.38  
Market cap. €25.2bn/US\$27.1bn  
Shares o/s 272m (ORD)  
Free float 67%  
Avg. daily volume ('000) 1,554  
Avg. daily value (m) €118.0  
Common s/h equity (12/15E) €27.5bn  
P/BV (12/15E) 0.9x  
Net debt / EBITDA (12/15E) NM

### EPS (UBS, diluted) (€)

	From	To	% ch	Cons.
12/15E	9.6	10.6	10	10.1
12/16E	12.7	12.9	2	12.0
12/17E	12.7	13.9	10	13.7

Consensus source: IBES/Bloomberg estimates. UBS EPS methodology is explained at the back of the document.

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Highlights (€m)	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
Revenues	41,270	40,932	41,055	45,236	50,127	52,574	54,950	56,976
EBIT (UBS)	122	(34)	1,105	2,128	2,916	2,938	2,787	2,871
Net earnings (UBS)	856	1,208	1,849	2,901	3,540	3,819	3,919	3,951
EPS (UBS, diluted) (€)	3.1	4.4	6.7	10.6	12.9	13.9	14.3	14.4
DPS (€)	1.9	1.7	1.9	2.6	3.2	3.1	3.3	3.4
Net (debt) / cash	1,492	1,761	2,104	2,406	3,107	3,444	3,796	4,211
Profitability/valuation	12/12	12/13	12/14	12/15E	12/16E	12/17E	12/18E	12/19E
EBIT margin %	0.3	-0.1	2.7	4.7	5.8	5.6	5.1	5.0
ROIC (EBIT) %	NM	NM	NM	NM	NM	NM	NM	NM
EV/EBITDA (core) x	-6.6	-3.7	-2.0	1.4	0.9	0.8	0.6	0.6
P/E (UBS, diluted) x	11.4	12.6	9.6	8.7	7.2	6.6	6.5	6.4
Equity FCF (UBS) yield %	(3.5)	(4.1)	(3.0)	6.4	5.6	4.7	4.2	6.6
Net dividend yield %	5.2	3.1	2.9	2.8	3.4	3.4	3.6	3.7

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of €92.57 on 19 Nov 2015 21:36 GMT

## PIVOTAL QUESTIONS

**Q: Can Renault deliver best-in-class organic growth as well as margin expansion?**

Yes. Renault is set to renew 30%-plus of its product portfolio over the next 12-18 months, mainly covering higher segments (C/D). "Sales to partners" should continue to contribute positively to the organic growth and support the utilisation rate in Europe. We estimate the weight of products on the CMF modular platforms will increase from 5% this year to 20% next year reaching 50%-plus by 2020.

[more](#) →**Q: Are we seeing the light at the end of the tunnel in emerging markets medium term?**

Risk is skewed to the upside, in our view. Assuming Brazil and Russia return to each weighing about 8-9% of Renault's unit sales, operations resume in Iran and China is off to a strong start, we quantify an incremental EPS contribution of around €1.5 to almost €15 in 2016E (10% impact vs UBS base case), all else remaining equal.

[more](#) →**Q: Will Renault continue to surf of the "low-cost" wave for longer?**

Yes. Renault recently launched the low-cost model in India (Kwid) and orders are already running well above production capacity and IHS expectations. All in all, we expect no meaningful competition for another few years (VW emissions scandal and end of Suzuki partnership could delay plans).

[more](#) →**Q: Is Renault well positioned for a strong start in China?**

Yes. Renault is well positioned for a strong start in China thanks to: (1) new products, which reduce the pricing pressure risk; (2) a clear focus on the fast-growing SUV segment; and (3) Nissan's past experience with the "copy and paste" strategy. We think the JV could rapidly deliver double-digit margins. However, direct earnings contribution is likely to remain low at c5% (c15% including Nissan).

[more](#) →

## UBS VIEW

Renault is well positioned to show best-in-class organic growth in Europe thanks to the new launches and "sales to partners". This should translate into higher margins and improving cash conversion.

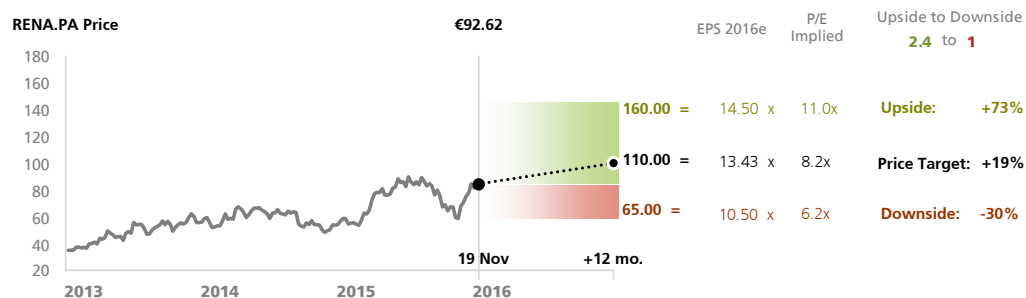
## EVIDENCE

**We publish today an [Evidence Lab report on China: Why the 'new normal' is better than feared](#).** The key conclusion of our consumer survey powered by Evidence Lab is that we expect mass JV brands, which are, on average, under-represented in SUVs, to take a bigger hit than domestic players. Renault is investing exclusively in SUVs, and targets tier 2 and tier 3 cities. In addition, our platform analysis confirms the potential to improve margins.

## WHAT'S PRICED IN?

We think the market is **not giving full credit on the organic growth potential** of Renault, despite the new launches. Consensus for next year remains below the "Drive the Change" target of €50bn. In addition, expectations regarding emerging markets remain very low, leaving scope for positive surprise.

## UPSIDE / DOWNSIDE SPECTRUM



Value drivers	Associate value	Auto operating margin	Emerging markets
€160 upside	Market value	5%	Brazil, Russia improvement
€110 target	Mid-point DDM	3%	No change versus current trends
€65 downside	Low-end DDM	1%	Further deterioration

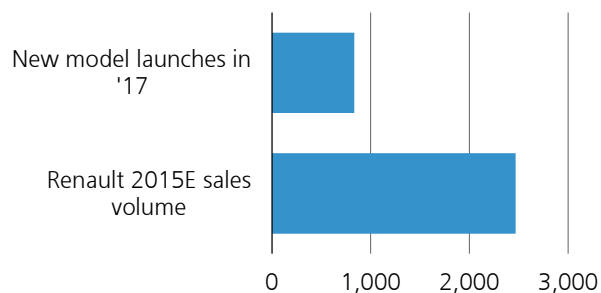
## COMPANY DESCRIPTION

Renault sold 2.71m vehicles in 2014 and has manufacturing operations in western/eastern Europe, Turkey, South Korea and LatAm, producing a range of passenger cars and LCVs.

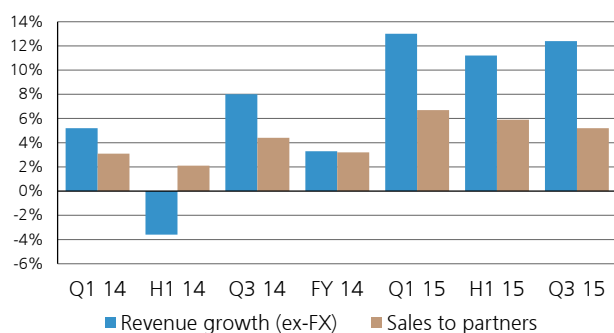
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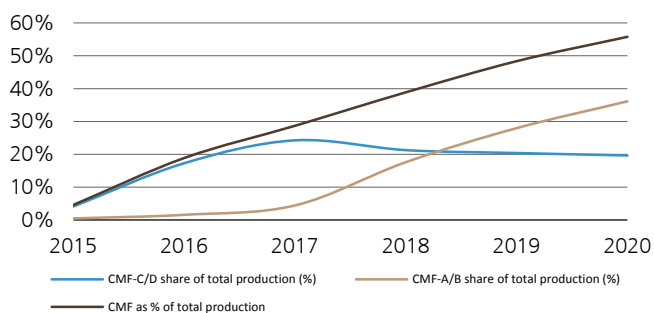
## OUR THESIS IN PICTURES

[return](#) ↑**Renault new model launches versus overall sales volumes ('000 units)**

Renault has one of the most active product portfolios over the next 12-18 months (in '17, new models should represent about 850k units (source: IHS) compared to sales of 2.5m in '15)

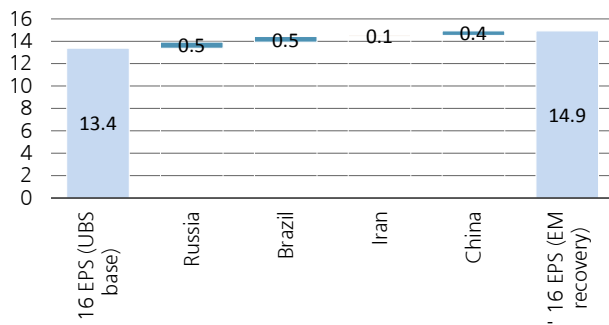
**Renault sales bridge: Revenue (excl FX) versus sales to partners contribution**

Sales to partners should continue to contribute positively to sales growth and support the utilisation rate in Europe

**Renault – % of total production on CMF modular platform**

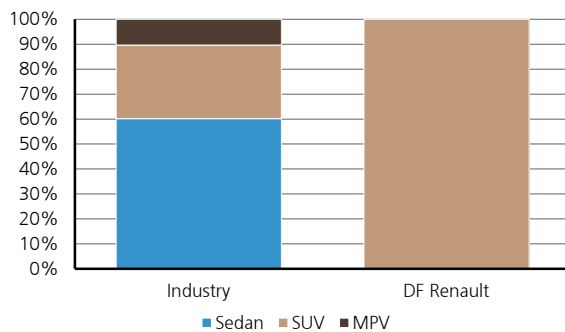
New launches mostly produced on CMF modular platform

### Emerging markets contribution (upside case, €)



In an upside case for EM, we estimate an incremental EPS contribution of around €1.5 to almost €15 in 2016 (versus UBS base case), all else remaining equal

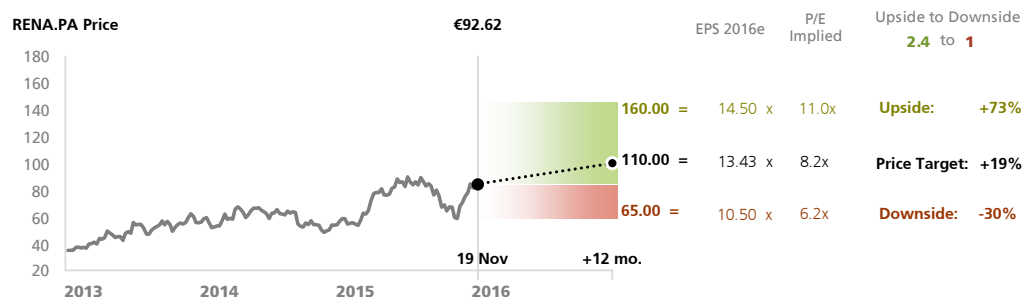
### Segment exposure by OEM (locally produced cars only)



Well positioned for a strong start in China

Sources for all exhibits above: Company data, UBS estimates, IHS Global Insight, China Auto Market

## UPSIDE / DOWNSIDE SPECTRUM

[return](#) ↑

Value drivers	Associate value	Auto operating margin	Emerging markets
€160 upside	Market value	5%	Brazil, Russia improvement
€110 target	Mid-point DDM	3%	No change vs current trends
€65 downside	Low-end DDM	1%	Further deterioration

**Risk to the current share price is heavily skewed to the upside**

Renault is trading at **€93** (as of 20 November).

**Upside (€160):** In our upside scenario, Renault generates an OP margin of 5%, a level at which Renault generates ROIC of 13%-plus versus normalised WACC of 9%. In such a scenario, core Renault is worth €100. Adding the market value of the stakes in associates Nissan and Daimler of €60 per Renault share (rather than the DDM value in our base case) would yield upside to €160.

**Base (€110):** Our PT is based on a DCF core value of €72 (3% long-term growth and margin) and the mid-point of our dividend income scenarios (€38).

**Downside (€65):** In our downside scenario, Renault fails to deliver the expected growth and OP margins decline to around 1%. In that case, low earnings and growth impair FCF generation, although balance sheet de-leveraging reduces the downside. Passing through the associate dividend received to shareholders also provides support. In our negative earnings scenario, we derive a core DCF value of €35, to which we add the low end of our DDM value from associates at €30. This suggests downside to €65.

## COMPANY DESCRIPTION

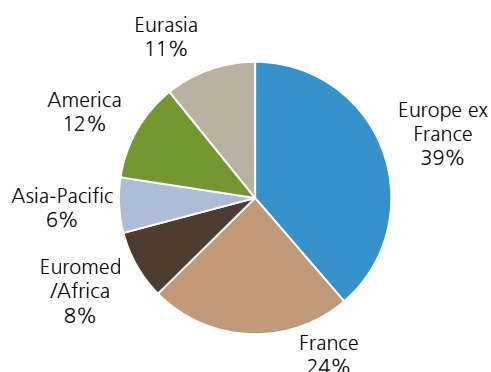
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<b>Market cap</b>	€27bn
<b>Shares outstanding</b>	296m (COM)
<b>Industry and outlook</b>	Automobile manufacturers
<b>Region</b>	Europe
<b>Website</b>	www.group.renault.com

Renault sold 2.71m vehicles in 2014 and has manufacturing operations in western/eastern Europe, Turkey, South Korea and LatAm, producing a range of passenger cars and LCVs. In addition to the Renault brand, it owns Dacia, a Romanian producer of low-cost cars, and Samsung Cars. Under cross-shareholding agreements, Renault owns a 43.4% stake in Nissan and a 1.55% stake in Daimler, while Nissan holds a 15% stake in Renault and 1.55% in Daimler. Renault-Nissan owns a 50% stake in Russian OEM AvtoVAZ, which Renault intends to consolidate at a future date.

**Industry outlook**

We have a constructive stance on European autos. The overall macro picture points to a continued recovery in Europe and an at least stable US market at high levels. Low commodities, FX tailwinds and an overall still favourable interest rate environment should also be supportive. The Chinese market should also do better than initially feared next year. On the negative side, regulatory cost keep rising in the sector, and R&D spending on technology mega-themes remains high. VW aside, we expect earnings growth across the board whilst valuation multiples remain below cycle-average. Our top picks are Daimler, Conti and Valeo.

**Revenues by region, 2014 (%)****EBIT by product segment (€m)**

	2012	2013	2014
Industrial	-606	-915	178
Financial services	754	747	751
<b>Group</b>	<b>148</b>	<b>-168</b>	<b>929</b>

Source for both exhibits: Company data

## PIVOTAL QUESTIONS

[return](#) ↑**Q: Can Renault deliver best-in-class organic growth as well as margin expansion?****UBS VIEW**

Renault is very well positioned to show best-in-class organic growth as well as margin expansion. We expect Renault to show revenue growth (excl FX) of 12+% driven 1) by new products, higher mix and pricing improvement and 2) "sales to partners" show a positive impact 4.5% next year (vs 5+% in '15). We stand 4% above consensus on sales and 10% above on EPS.

**EVIDENCE**

Organic growth drivers: Busy product renewal over the next 12-18 months (30%-plus of product portfolio renewed), which is mainly covering higher segments (C/D). The contribution from "sales to partners" (Daimler/Nissan) should stay at high levels (c50% of revenue growth so far this year). Margin expansion drivers: New launches should support product mix/pricing and are produced on the CMF modular platform (from 5% of total production this year to 20% next year, reaching 50%-plus by 2020E). "Sales to partners" should continue to boost the utilisation rate in Europe.

**WHAT'S PRICED IN?**

We think the market is not giving full credit on the organic growth potential of Renault, despite the new launches. Consensus for next year remains below the "Drive the Change" target of €50bn.

**Best-in-class organic growth...****Driver 1: New product launches**

Renault is set to renew 30+% of its product portfolio over the next 12-18 months, mainly covering higher segments. Therefore, we expect the average pricing to improve due to higher product mix. The "Megane" replacement should also be an important contributor to volume and net pricing next year. We believe Renault had to offer higher content per car, without being able to fully price it to end customers, for the old Megane in order to stay competitive against more recent VW Golf and Peugeot 308, for instance.

**New launches should support product mix and pricing**



**Figure 1: Renault has one of the most active product portfolios over the next 12-18 months**

Launch date	Product	Comment
Q4 14	Espace	Much higher mix than anticipated First Renault to use the CMF platform
Q2 2015	Kadjar	First crossover in the C-segment based on CMF C-D platform Same platform as second generation Nissan Qashqai Replacing Koleos To be launched in China, early '16
Q3 15	Kwid	Break through entry vehicle for Emerging markets Built in India; may also be built in Brazil Produced on the CMF-A platform to be used by Nissan 50,000 bookings in India, much higher than production capacity Average selling price: €4,000-5,000 First attempt to compete with Maruti Suzuki
Q4 15/Q1 16	Megane	Two models: GT and regular hatchback 6 engines available at launch (3 petrol, 3 diesel) Estate launched in '16
Q4 15	Talisman	Replacing the Laguna, D-segment Produced in Douai, France Estate version available in H1 2016
2016	Oroch	Entering the pick up truck market Penetrate the Brazilian market and support market coverage Dacia Duster pick-up
H1 16	Alaskan	Pick up truck Shared on Nissan platform Mainly for SA
2016	Renault D-CUV	New mid-size crossover for Europe and China Based on Nissan's X-Trail
2016	Renault B-SUV	
2016	Scenic	Fourth generation compact MPV

Source: IHS Global Insight, UBS estimates, Press

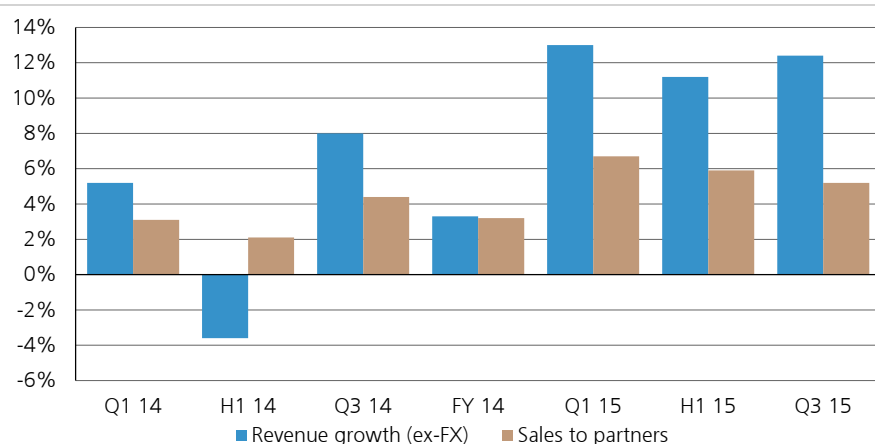
## Driver 2: Sales to partners

Over the past few quarters, "sales to partners" have been very strong, contributing 5+pts of sales growth, or 50+% of the automotive division's sales growth. Renault management guides for a reduced contribution over the coming quarters due to a more challenging base. We expect "sales to partners" to continue to contribute positively to the group's growth, which is quite important for the coverage of the fixed cost base as "sales to partners" should contribute 12pts of the planned utilisation rate improvement in Europe through the "Drive the change" plan (after 2016). We expect next year "sales to partners" to show a positive impact of slightly less than 5% to revenue growth (vs 2015: 5+%).

Renault expects "sales to partners" to double during the life of Renault's "Drive the change" plan (€400m contribution to sales in '13, €1.2bn in '14 and €1.5bn ytd) thanks to selling cars to Nissan/Daimler (Smart, Citan, Rogue), engine/powertrain (mainly diesel) and gear boxes, deal with Fiat for mid light commercial vehicles (from end '15).

**Figure 2: Renault sales bridge: revenue (excl. FX) vs sales to partners contribution**

"Sales to partners" have contributed about half of the revenue growth (excl. FX)



Source: Company data, UBS estimates

**Figure 3: Monthly performance of Renault and "partners"**

y/y growth rates	Jan-15	Feb-15	Mar-15	Q1 15	Apr-15	May-15	Jun-15	Q2 15	Jul-15	Aug-15	Sep-15	Q3 15	Oct-15
<b>Worldwide</b>	-3%	-4%	7%	1%	4%	-5%	3%	1%	1%	2%	1%	1%	2%
Europe	9%	8%	12%	10%	13%	6%	6%	8%	3%	10%	8%	6%	0%
Dacia	7%	-2%	7%	4%	13%	1%	5%	6%	-6%	-11%	8%	-3%	-9%
Renault brand	10%	11%	13%	12%	13%	8%	7%	9%	6%	18%	8%	10%	3%
M0	-10%	-16%	-1%	-9%	-1%	-9%	5%	-2%	-2%	-4%	1%	-2%	7%
<b>Partners in Europe</b>													
Nissan	35%	27%	21%	26%	9%	14%	24%	16%	62%	19%	24%	33%	-4%
Daimler	15%	14%	20%	17%	8%	12%	22%	14%	72%	25%	19%	35%	21%
MB	12%	10%	16%	14%	3%	5%	17%	8%	63%	19%	13%	28%	11%
Smart	134%	45%	57%	76%	56%	84%	88%	75%	11%	117%	131%	86%	216%

Source: Company data, UBS estimates, ACEA

Note: Low cost platform (M0/B0): Dacia models (all produced on low cost platform): Dokker, Duster, Lodgy, Logan, Sandero. Renault models produced on the low cost platform: Dokker, Duster, Kwid, Logan and Sandero.

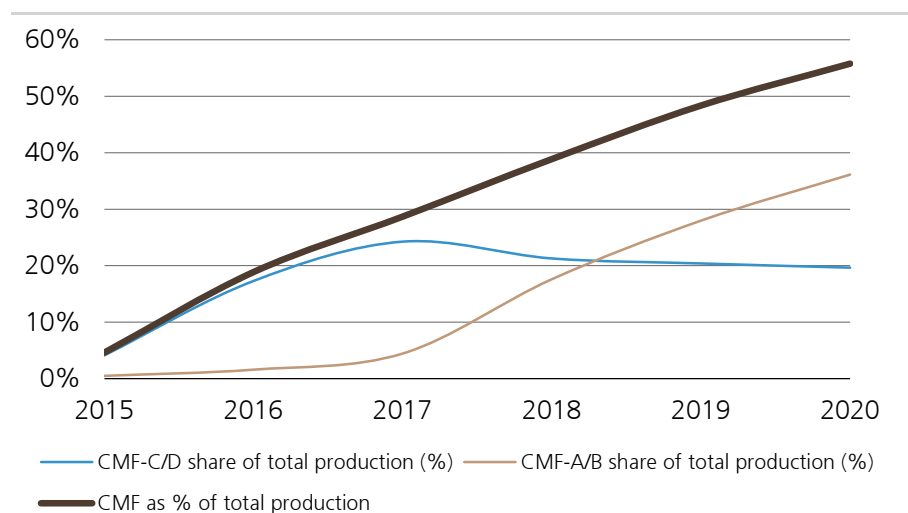
## ...should support margin expansion

### New launches mostly produced on CMF modular platforms

This year, we estimate that "only" 5% of Renault production is on the CMF platform (mainly C/D). We expect this number to reach 20% as early as next year thanks to new product launches and 50+% by 2020.

Renault expects the CMF platform to generate 30-40% average cost reduction (R&D and Capex) for entry models and 20-30% lower purchasing costs.

**Figure 4: Renault - % of total production on the CMF modular platform**



Source: IHS Global Insight, UBS estimates

Note: models produced on the **CMF C/D platform** are D-CUV, D-Sedan, Espace, Fluence, Kadjar, Megane, QM5, Scenic, SM3, SM7, Talisman; models produced on the **CMF A/B platforms** are A-Van Kwid, B-CUV, Captur, Clio, Duster, Duster Oroch, Lodgy, Logan MCV, Pulse, Scala, Symbol, Tondar, Zoe

## PIVOTAL QUESTIONS

[return](#) ↑**Q: Seeing the light at the end of the tunnel in emerging markets?****UBS VIEW**

While we think it is too early to turn bullish on emerging markets, we note 1) Renault delivery has been impressive in markets which have turned much worse than expected and 2) the risk is currently skewed to the upside.

**EVIDENCE**

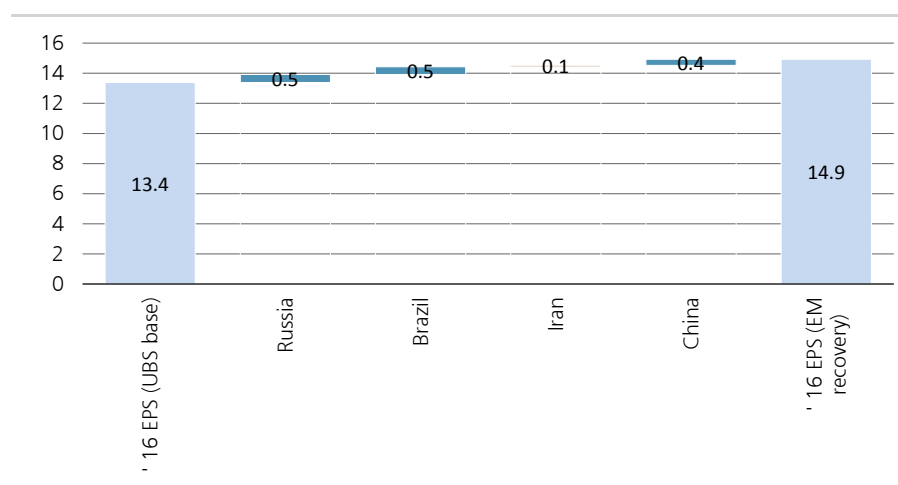
Assuming Brazil and Russia return to each weighing about 8-9% of Renault's unit sales (from 7% and 4%, respectively), operations resume in Iran and China is off to a strong start, we estimate an incremental EPS contribution of €1.5 €15 in 2016 (c10% positive impact vs UBS base case), all else remaining equal.

**WHAT'S PRICED IN?**

Expectations regarding emerging markets remain very low, leaving scope for positive surprise. We believe the current share price does not reflect any improvement in the near term.

**Emerging markets risk skewed to the upside**

While we think it is too early to turn bullish on emerging markets, we note 1) Renault delivery has been impressive in markets which have turned much worse than expected and 2) the risk is currently skewed to the upside. Assuming Brazil and Russia return to each weighing about 8-9% of Renault's unit sales (from 7% and 4%, respectively), operations resume in Iran and China is off to a strong start, we estimate an incremental EPS contribution of €1.5 €15 in 2016 (c10% positive impact vs UBS base case), all else remaining equal.

**Figure 5: EPS bridge in a upside case for emerging markets**

Source: UBS estimates

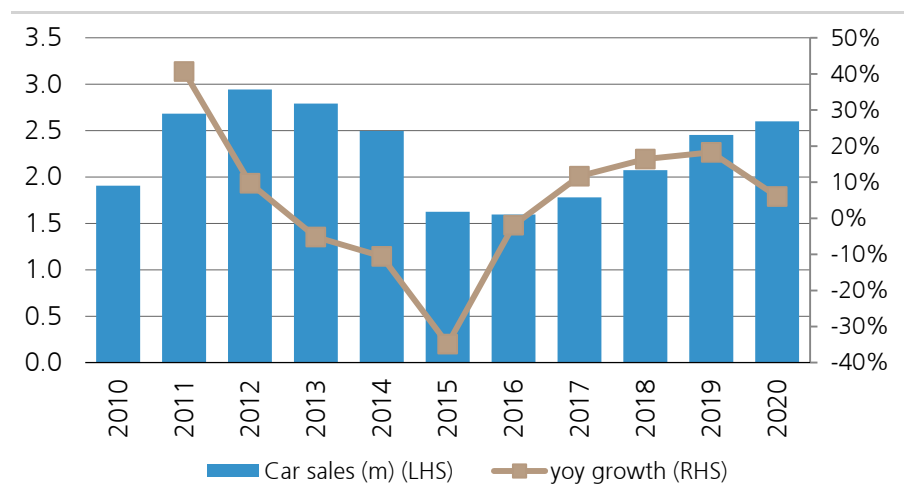
## Stabilising Russia should also help the group's EBIT margin

During the Q3 call, Renault management highlighted that Russia was showing some signs of stabilisation and there could be some positive news over the coming months. As highlighted in Figure 6, the market is currently running almost 50% below 2012 levels and is expected to rebound next year.

In our view, Renault managed the drop in new car sales very well thanks to 1) a high localisation rate (minimise FX exposure, avoid custom duties and save on logistics costs), 2) a highly flexible costs base and 3) a clear focus on prices.

Russia used to represent about 8% of Renault worldwide sales (vs 4% currently) and generate margins well above the group average.

**Figure 6: Russia new car sales**



Source: IHS Global Insight, UBS estimates

## PIVOTAL QUESTIONS

[return](#) ↑**Q: Surfing on the "low-cost" wave for longer****UBS VIEW**

We view the "low-cost" strategy as very compelling in terms of the returns it generates. Threats from new entrants are unlikely for about another two years.

**EVIDENCE**

VW plans on the low cost may be delayed due to the end of the partnership with Suzuki and the emissions scandal. The Kwid launch in India seems to be a success with orders (50+k) running well above production capacity and IHS expectations (16k expected for this year).

We view the "low-cost" strategy as very compelling in terms of the returns it generates. This segment is likely to become more competitive over the coming years as it attracts new entrants. Having said this, there is a possibility that VW's plans (Renault's main threat) in this field are delayed due to the end of the partnership with Suzuki and the emissions scandal.

The launch of the Kwid in India is quite promising. Since the launch just a few months ago, the orders are running well above the current capacity. For instance, IHS Global Insight expects volume of 16k units for this year and 70k units for next year, compared to orders running above 50k units.

**Figure 7: At least another two years without meaningful competition in "low cost" cars**

2015	2016	2017	2018	2019
No meaningful competition			VW competition at the earliest	

Source: UBS

## PIVOTAL QUESTIONS

[return](#) ↑**Q: Well positioned for a strong start in China?****UBS VIEW**

We estimate direct earnings contribution potential to be around €0.5/share (200k cars sold at an average selling price of €12k generating an EBIT margin of 13%), or less than 5% of our '16 EPS estimate.

**EVIDENCE**

While we think it is too early to turn bullish on emerging markets, data in our Evidence Lab report suggests that Renault is investing in the right segment (SUV) and locations (tier 2 and 3 cities) in China. Leveraging Nissan's past experience with the "copy and paste" strategy should allow the JV to rapidly deliver double-digit margins (we assume 10-15%).

**WHAT'S PRICED IN?**

Renault is just starting operations in China. Therefore, the current share price reflects limited impact from China.

**Renault's "Copy and Paste" strategy in China**

Since '13, Renault has operated in a 50/50 JV with DongFeng ("DF") with total equity of RMB4bn. During Phase 1, the overall strategy is based on segment selectivity (mainly SUV) to improve brand awareness and maximise profitability (requirement by local authorities to be profitable) in order to obtain approval for Phase 2 and potentially expand the range to Sedans. Throughout the process, the strategy is to leverage as much as possible Nissan's operations/experience in China ("copy and paste").

In Phase 1, the initial capacity target is 150k units (to be reached by '17) and imports maintained at c35k units. Product plan: Kadjar (6 months after European launch with some local specificities; 85% localisation rate); Captur (end of '15; sourced from Europe); D-crossover (end of 15/beg 16). EV launch and local brand strategy remain under study. Renault targets 6% market share in its segment and expects the overall market to grow 4.5-6% annually.

Production process, equipment and machineries are optimised using Nissan's experience in order to maximise profitability. However, Renault was required to build its own engine factory.

**Product strategy based on full SUV line-up**

**Synergies and "copy/paste" strategy**

**Renault's indirect exposure via Nissan**

Renault has a direct exposure to China via its 43%-stake in Nissan. We estimate China represents between 20% and 25% of Nissan earnings. Therefore, the indirect to China stand at about 10%. Nissan is our Japanese top pick on two new model launches in the ≤1.6L engine segment. Nissan also has a strong product portfolio in the compact SUV segment (launch of Murano (D SUV) and Qashqai (C SUV) planned at end 2015).

## What is Evidence Lab telling us about China?

Today, we publish an Evidence Lab report: *"Why the 'new normal' is better than feared"*, including a consumer survey focussing on China. The key conclusion for us is we do not expect a margin collapse for car makers but diverging trends between segments. We expect mass JV brands, which are on average under-represented in SUVs, to take a bigger hit than domestic players. We think the mass brand segment, sedans (RMB100-200k segments) will suffer most, and compact mass brand SUVs will suffer least. Renault is investing in the right segment (SUV) and locations (tier 2 and 3 cities) in China.

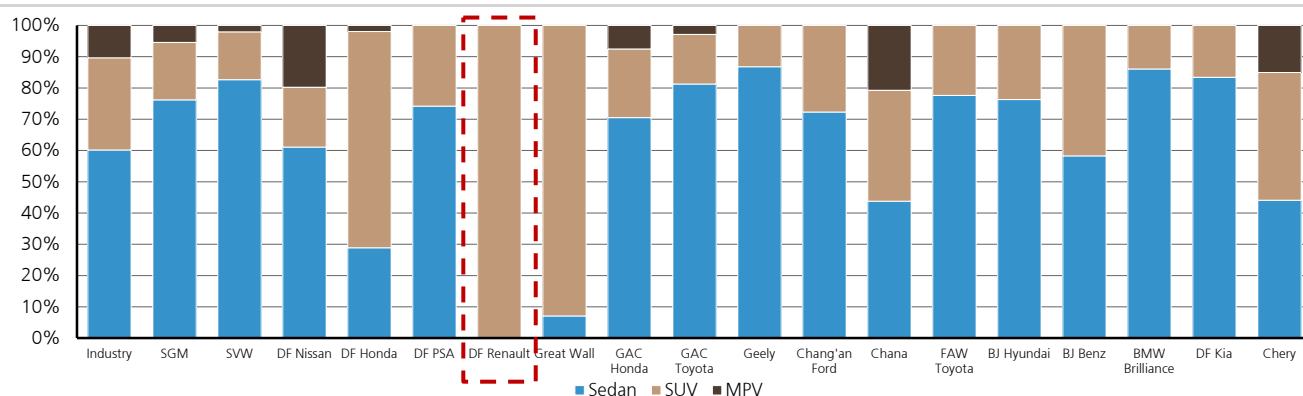
For this report, UBS Evidence Lab conducted an online survey with 1,342 Chinese consumers aged between 21-54 years who reside in Tier 1 (Beijing, Shanghai, Guangzhou and Shenzhen), Tier 2 and Tier 3 cities across China to understand their purchase motivations, considerations and thought process in planning for a car purchase in the next 12 months. The survey, conducted from September 20 to October 1, also helps to better understand their financial position, preference towards financing the purchase and sentiment towards the economy. Our conclusions based on the sample have a potential sampling error of +/-2.22ppt at a 90% confidence level.

The SUV segment remains the growth engine with an expected increase in sales by 25% y/y in 2016 due to continued shift in consumer preferences (confirmed by Evidence Lab). OEMs with strong SUV portfolios should continue to outperform.

Renault is set to remain a niche player in China. However, we think Renault is well positioned for a strong start given 1) launching new products exclusively in the SUV segment and 2) focussing mainly on Tier 2 and Tier 3 cities and 3) leveraging Nissan's know-how as much as possible.

**Well positioned for a strong start in China**

**Figure 8: Segment exposure by OEM (locally produced cars only)**



Source: China Auto Market, UBS

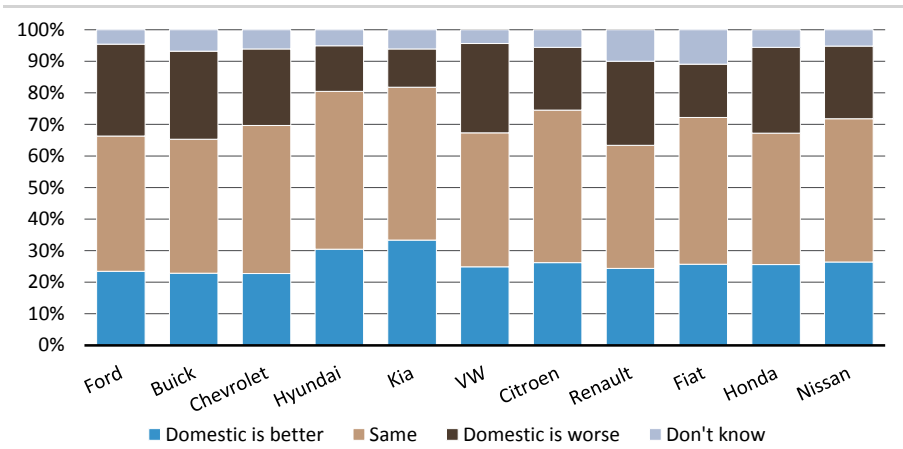
Our Evidence Lab survey results show that Chinese consumers still prefer to buy international brands over domestic makes, all else equal. That's good news for international mass market brands. Bad news is that the premium paid for is likely to shrink. Given that domestic brands usually have lower plant utilisation rates than the JV's (and therefore will remain more aggressive on pricing), we see JV margins under pressure. So far, the average price difference between popular JV and domestic models is 25-30%, according to our research. In the SUV segment, the price difference is sometimes as high as 50% for comparable models. The survey suggests that 62% would prefer the best domestic car over a JV model if

**Premium paid for international brands is likely to shrink**



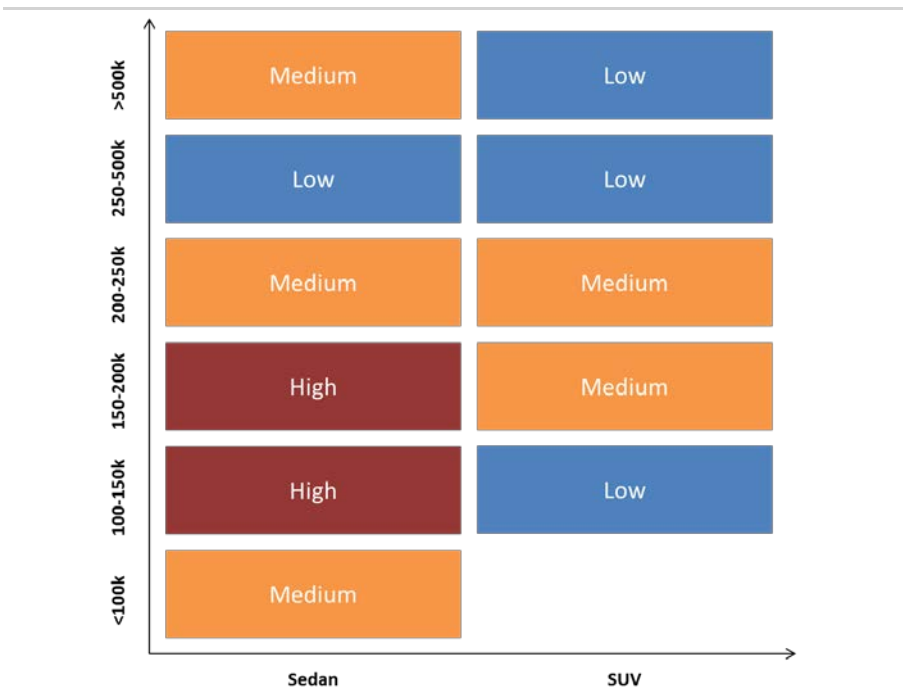
the price point is at least 20% lower. At the same price, only 10% would opt for the domestic make.

**Figure 9: Best domestic brands seen at similar quality to JV brands – Hyundai, Kia, Fiat and Citroen even seen worse than domestic**



Source: UBS Evidence Lab

**Figure 10: Price Wars – the UBS heat map for 2016E**



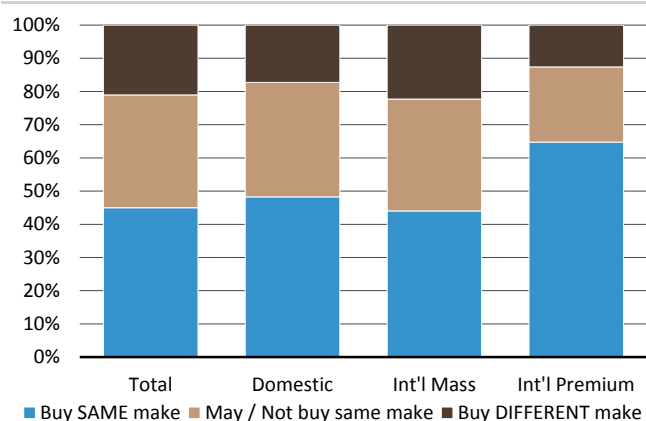
Source: UBS estimates

Note: Low = up to -3%, Medium = -3 up to -5%, High = worse than -5%.

Brand loyalty remains low in the mass market segment, which makes price competition more intense. Surprisingly, loyalty is the lowest amongst owners of JV mass brands, but domestic brands are not doing much better. The premium segment enjoys the highest brand loyalty, although rates are clearly lower than in mature markets.

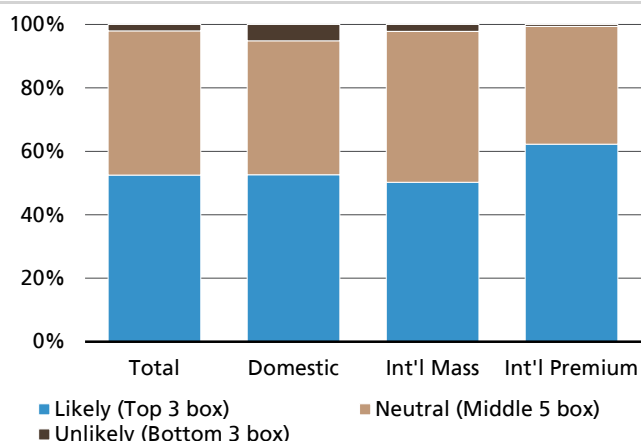
**Low brand loyalty in mass market brands; more at risk of domestic brand competition**

**Figure 11: Owners – likelihood to buy same brand again**



Source: UBS Evidence Lab

**Figure 12: Owners – likelihood to recommend to friends**



Source: UBS Evidence Lab

Another aspect playing in favour of Chinese domestic players is that the desire for SUVs can be better met with domestic brands, given the budget constraints of buyers. Our survey shows that the average budget for a domestic car is RMB124k, which is sufficient to buy a popular SUV model, such as the Haval H6 from Great Wall (which is the most-preferred domestic SUV model on sales figures and our survey). On the other hand, the budget for a JV car is RMB 161k on average, and only 21% of potential JV brand buyers have a budget >RMB200k. The VW Tiguan, Volkswagen's only SUV in China, sells between RMB200-240k. We believe that clients may increasingly give priority to the type of car over the brand. In terms of factors that impact make and model, the slower economic growth is seen as a key driver by respondents. This would also play into the hands of the domestic brands.

## Estimates and consensus

Post stronger Q3 sales and higher contribution from Nissan to Renault earnings for the quarter, we raise earnings estimates by c10% for this year.

**Figure 13: Renault – Change of estimates (€m/€)**

	2015E			2016E		
	New	Old	% change	New	Old	% change
Group revenues	45,236	45,165	0%	50,127	49,556	1%
Operating margin	2,228	2,135	4%	3,016	2,772	9%
EBIT	2,128	2,035	5%	2,916	2,672	9%
Income from associates (Nissan, Avtovaz)	1,744	1,544	13%	1,828	1,977	-8%
Net income	3,057	2,792	9%	3,722	3,682	1%
EPS reported	10.96	9.99	10%	13.38	13.24	1%
EPS (UBS adjusted)	10.58	9.59	10%	12.92	12.72	2%
Net industrial debt / (cash)	-2,406	-2,327	3%	-3,107	-2,881	8%

Source: UBS estimates

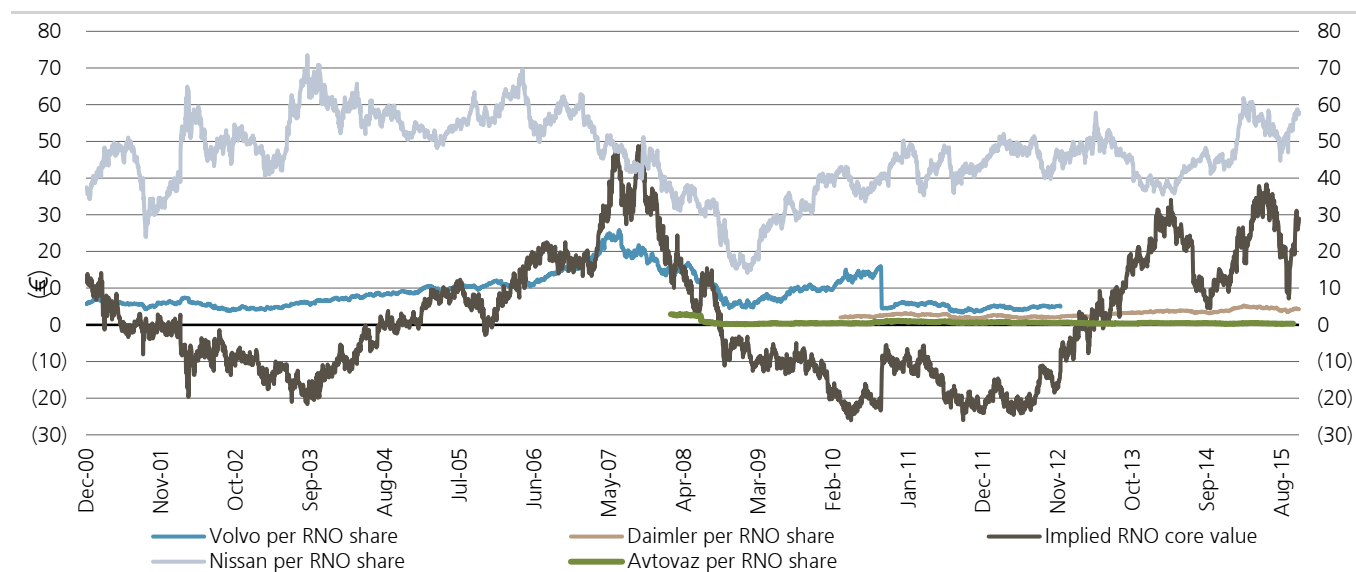
**Figure 14: Renault – UBS vs consensus**

in MEUR	FY 2015		FY 2016	
	UBSe	Consensus	UBSe	Consensus
Group Revenues	45,236	44,986	50,127	48,204
UBS vs consensus		1%		4%
Group Operating margin	2,228	2,199	3,016	2,727
Operating margin % revenues	4.9%	4.9%	6.0%	5.7%
UBS vs consensus		1%		6%
EPS	11.0	10.3	13.4	12.2
UBS vs consensus		6%		10%

Source: UBS estimates

## Valuation

Figure 15: Renault implied core value per share back at €29



Source: Datastream, UBS estimates

# Financials

Figure 16: Renault financials (€m/€)

Group P&L	2011	2012	2013	2014	2015E	2016E	2017E	2018E	2019E
Group revenue	42,628	41,270	40,932	41,055	45,236	50,127	52,574	54,950	56,976
% change	9.4%	-3.2%	-0.8%	0.3%	10.2%	10.8%	4.9%	4.5%	3.7%
COGS	(34,759)	(34,092)	(33,611)	(33,310)	(36,203)	(39,587)	(41,591)	(43,745)	(45,478)
Gross margin	18.5%	17.4%	17.9%	18.9%	20.0%	21.0%	20.9%	20.4%	20.2%
R&D	(2,027)	(1,915)	(1,812)	(1,721)	(1,874)	(2,109)	(2,267)	(2,439)	(2,431)
SG&A	(4,751)	(4,534)	(4,267)	(4,415)	(4,931)	(5,414)	(5,678)	(5,880)	(6,096)
Operating margin	1,091	729	1,242	1,609	2,228	3,016	3,038	2,887	2,971
% of revenue	2.6%	1.8%	3.0%	3.9%	4.9%	6.0%	5.8%	5.3%	5.2%
Other operating items	153	(607)	(1,276)	(504)	(100)	(100)	(100)	(100)	(100)
EBIT	1,244	122	(34)	1,105	2,128	2,916	2,938	2,787	2,871
Net interest	(219)	(267)	(267)	(282)	(226)	(194)	(160)	(147)	(130)
Other financial items	98	1	(15)	(51)	0	0	0	0	0
Associates	1,524	1,504	1,444	1,362	1,744	1,828	2,033	2,187	2,219
EBT	2,647	2,284	1,128	2,134	3,646	4,551	4,811	4,827	4,960
Tax	(508)	(549)	(433)	(136)	(589)	(829)	(841)	(799)	(830)
Net income	2,139	1,735	695	1,998	3,057	3,722	3,970	4,027	4,130
Minority	(47)	37	(109)	(108)	(54)	(54)	(53)	(52)	(51)
Reported EPS	7.68	6.51	2.14	6.90	10.96	13.38	14.29	14.50	14.88
Adjusted EPS	6.96	3.14	4.41	6.75	10.58	12.92	13.93	14.30	14.41
Industrial cash flow	2011	2012	2013	2014	2015	2016	2017	2018	2019
Industrial net income	1,975	1,576	376	1,755	2,500	3,122	3,364	3,442	3,534
Associates and non recurring	(1,518)	(1,495)	(1,430)	(1,366)	(1,744)	(1,828)	(2,033)	(2,187)	(2,219)
Dividend received									
PP&E depreciation	2,049	2,230	2,413	2,029	1,787	1,738	1,718	1,798	1,952
Amortisation of R&D and intangibles	771	790	751	673	701	734	702	801	732
Other	(367)	(524)	804	47	0	0	0	0	0
Cash earnings	2,910	2,577	2,914	3,138	3,245	3,766	3,752	3,854	3,999
Change in net working capital	627	922	790	596	135	273	137	133	113
Operating cash flow	3,537	3,499	3,704	3,734	3,380	4,039	3,888	3,987	4,112
Gross PP&E capex	(1,564)	(1,936)	(1,914)	(1,541)	(1,892)	(2,149)	(2,257)	(2,361)	(2,341)
Gross investment in intangibles	(887)	(900)	(827)	(964)	(899)	(967)	(893)	(932)	(964)
Disposals	239	162	198	89	100	100	100	100	100
Operating FCF	1,325	825	1,161	1,318	689	1,022	839	794	907
Acquisitions and change in other financial assets	(244)	1,089	(179)	(342)	0	0	0	0	0
Dividends received	335	507	433	463	588	681	666	728	743
Dividends paid	(88)	(338)	(539)	(503)	(555)	(715)	(866)	(856)	(909)
Change in net debt	993	1,576	443	473	134	307	(28)	(62)	(2)
Financing	(2,164)	0	0	0	0	0	0	0	0
Change in cash & equivalents	(1,171)	1,576	443	473	134	307	(28)	(62)	(2)
Industrial balance sheet - Finco at equity	2011A	2012	2013	2014	2015E	2016E	2017E	2018E	2019E
PP&E assets	11,357	11,534	11,035	10,547	10,652	11,063	11,601	12,165	12,554
Intangible assets	3,676	3,382	3,194	3,328	3,475	3,659	3,799	3,879	3,147
Equity investments	18,495	18,164	17,758	19,806	21,076	22,363	23,874	25,476	27,089
Other investments and financial assets	3,237	3,433	4,036	4,353	4,353	4,353	4,353	4,353	4,353
Deferred tax asset	1,007	1,047	1,301	1,663	1,663	1,663	1,663	1,663	1,663
Other non current assets	497	348	368	514	514	514	514	514	514
Total non current assets	38,269	37,908	37,692	40,211	41,733	43,614	45,805	48,050	49,321
Inventories	4,409	3,825	3,121	3,361	3,887	4,318	4,534	4,744	4,923
Receivables	1,354	1,195	1,031	1,409	1,573	1,747	1,835	1,919	1,992
Current financial assets	1,441	1,150	975	1,143	1,143	1,143	1,143	1,143	1,143
Loans and marketable securities	1,605	1,583	1,604	1,805	1,805	1,805	1,805	1,805	1,805
Cash and equivalents	7,618	10,072	10,704	11,591	11,742	12,092	12,261	12,437	12,644
Total current assets	16,427	17,825	17,435	19,309	20,150	21,106	21,578	22,049	22,507
Total assets	54,696	55,733	55,127	59,520	61,883	64,720	67,383	70,098	71,828
Shareholders' equity	26,586	27,053	25,735	27,324	29,905	32,552	35,294	38,123	40,543
incl industrial operations	24,046	24,403	22,836	24,188	26,655	29,162	31,760	34,446	36,729
incl financing operations	2,540	2,650	2,899	3,136	3,250	3,389	3,534	3,676	3,814
Minority interests	481	255	377	422	476	530	583	635	686
Deferred tax liability + LT provisions	2,058	2,262	2,277	2,598	2,900	3,222	3,383	3,539	3,673
Non current debt	6,066	6,362	6,837	7,272	7,121	6,771	6,602	6,426	6,219
Other non current liabilities	340	424	691	779	870	966	1,014	1,061	1,101
Total non current liabilities	35,531	36,356	35,917	38,395	41,272	44,040	46,876	49,784	52,222
ST provision for risks	833	857	1,067	1,114	1,171	1,234	1,264	1,293	1,317
Current debt	3,789	3,716	3,446	3,872	3,872	3,872	3,872	3,872	3,872
Trade and other payables	6,402	6,663	6,349	7,094	7,919	8,797	9,237	9,664	10,029
Other liabilities and deferred income	8,141	8,141	8,348	9,045	7,650	6,778	6,134	5,486	4,389
Total current liabilities	19,165	19,377	19,210	21,125	20,611	20,680	20,507	20,314	19,607
Total equity and liabilities	54,696	55,733	55,127	59,520	61,883	64,720	67,383	70,098	71,828
Reported net industrial debt/(cash)	299	(1,492)	(1,761)	(2,104)	(2,406)	(3,107)	(3,444)	(3,796)	(4,211)

Source: Company data, UBS estimates

### Forecast returns

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Forecast price appreciation	+18.8%
Forecast dividend yield	3.4%
Forecast stock return	+22.2%
Market return assumption	4.7%
Forecast excess return	+17.5%

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### UBS EPS and consensus EPS

The UBS EPS is an adjusted diluted EPS metric. It is calculated using the UBS analyst's interpretation of earnings suitable for valuation purposes divided by the diluted number of shares. This may differ to the way the consensus EPS metric has been calculated.

### Statement of Risk

The automobile sector has in the past exhibited high levels of volatility in terms of profitability and valuation. Sector earnings and performance are highly sensitive to variations in volume, pricing, raw material costs and currency, all of which have been volatile recently. Long-term structural trends continue to improve as a result of higher demand in EM, early signs of sector concentration improving and structurally lower currency exposure but near-term cyclical drivers have become more challenging after several years of strong earnings and share price performance. We are also concerned that in a macro recovery rising interest rates would become a material headwind for the industry.

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12-Month Rating	Definition	Coverage <sup>1</sup>	IB Services <sup>2</sup>
Buy	FSR is > 6% above the MRA.	49%	33%
Neutral	FSR is between -6% and 6% of the MRA.	40%	26%
Sell	FSR is > 6% below the MRA.	12%	18%
Short-Term Rating	Definition	Coverage <sup>3</sup>	IB Services <sup>4</sup>
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	less than 1%	less than 1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	less than 1%	less than 1%

Source: UBS. Rating allocations are as of 30 September 2015.

1:Percentage of companies under coverage globally within the 12-month rating category. 2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

3:Percentage of companies under coverage globally within the Short-Term rating category. 4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

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**UBS Limited:** David Lesne; Chervine Golbaz. **UBS AG:** Patrick Hummel, CFA.

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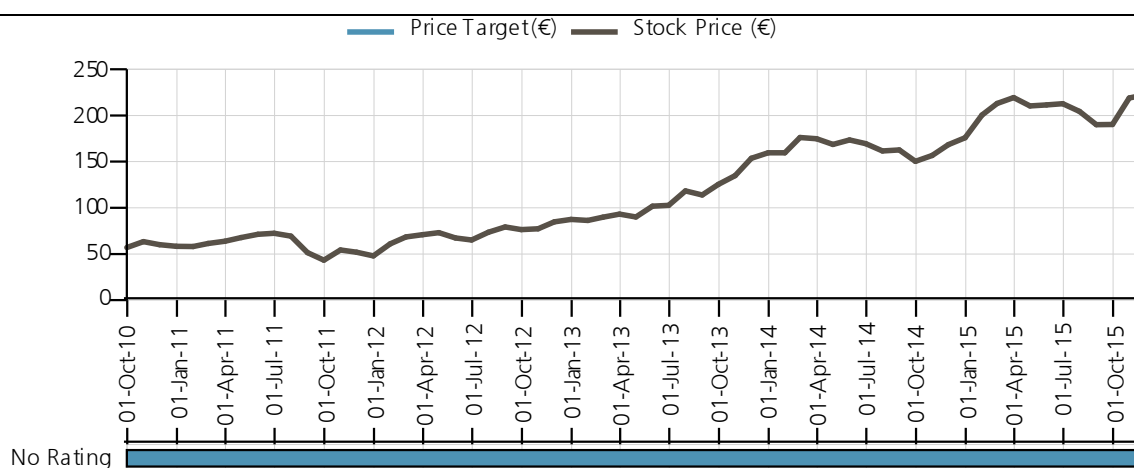
Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
<b>Conti</b>	CONG.F	Not Rated	N/A	€221.35	20 Nov 2015
<b>Daimler</b>	DAIGn.DE	Neutral	N/A	€79.25	20 Nov 2015
<b>Renault SA</b>	RENA.PA	Buy	N/A	€93.02	20 Nov 2015
<b>Valeo</b>	VLOF.PA	Buy	N/A	€143.90	20 Nov 2015

Source: UBS. All prices as of local market close.

Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

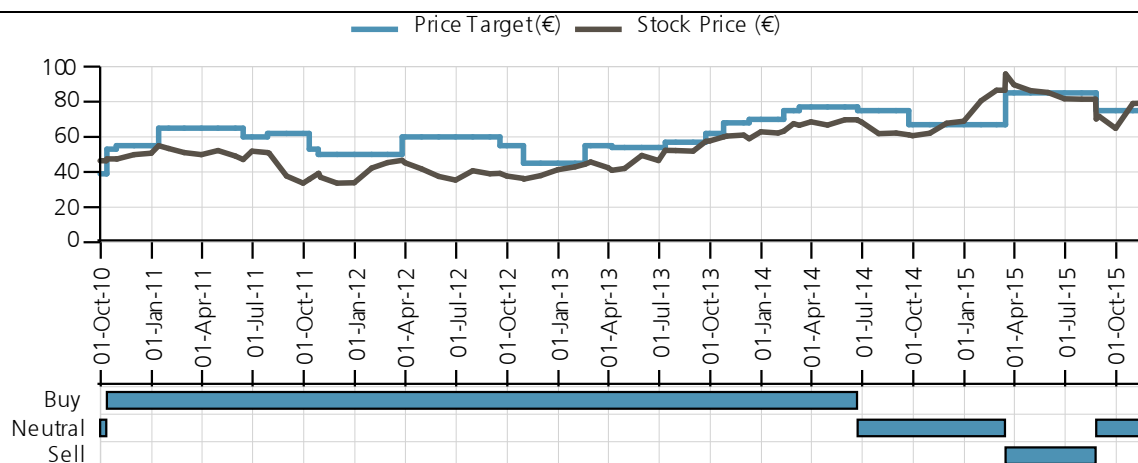
Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

### Conti (€)



Source: UBS; as of 20 Nov 2015

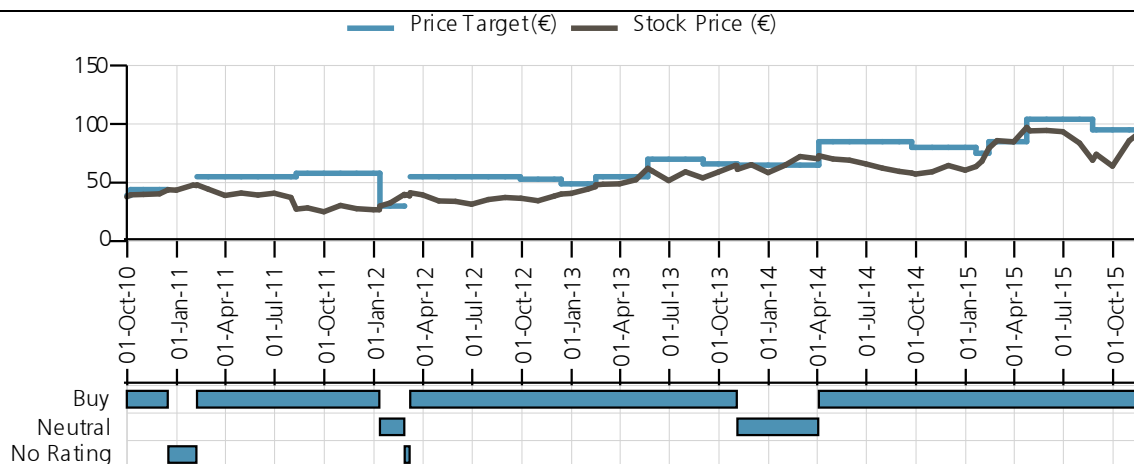
### Daimler (€)



Source: UBS; as of 20 Nov 2015

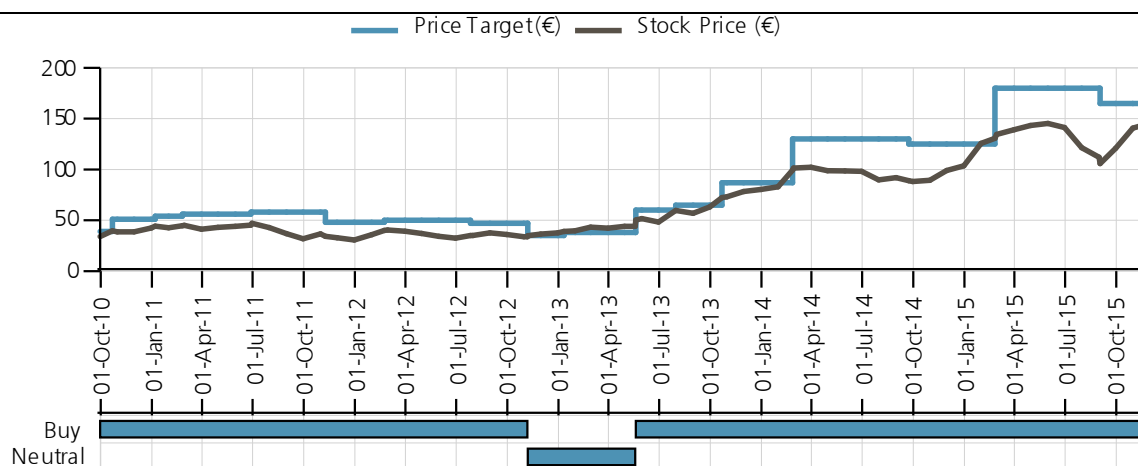


## Renault SA (€)



Source: UBS; as of 20 Nov 2015

## Valeo (€)



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