GLOBAL IDEAS

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Hyundai Motor Company: Speeding ahead

Investment summary:

- Hyundai Motor Company is a South Korean automobile manufacturer which, along with its subsidiaries, operates in three business divisions: vehicle, financial (financing services and credit cards) and other business (construction of railways, steel manufacturing and others).
- The group has seen phenomenal growth in vehicle sales and despite the difficult global operating environment in FY12 it sold 4.41mn units – 120,000 units more than its 4.29mn business target. Even in Europe where vehicle sales are falling, Hyundai experienced growth – its market share in the region has grown from 2.9% in 2011 to 3.5% in 2012 while competitors such as Volkswagen (VW) and Toyota were unable to grow their operations in Europe.
- Since it debuted in China a decade ago Hyundai's cumulative car sales have exceeded the 7mn mark and in early September it reported sales of 1mnn units in China YTD -- the fastest pace since it entered that market. In the US, Hyundai's facility in Alabama set an annual production record of 361,348 units in FY12, which was still not enough to satisfy the robust demand (which in the end cost the company market share).
- Hyundai has a rapidly growing reputation and brand value and in terms of profitability its FY12 operating margin is close to 10% - the highest amongst its competitors with the exception of premium vehicle manufacturer Bayerische Motoren Werke AG (BMW) at c. 10.9%.
- On the negative side, because Hyundai earns over half its revenue outside South Korea it is exposed to exchange rate fluctuations which can have an impact on the group's sales, earnings and cash flow. It also has capacity constraints in the US.
- Negative publicity on the back of product recalls and labour disputes with its union in South Korea has also weighed on the company.
- Compared with Ford, Nissan, BMW and VW, Hyundai is trading at higher current P/E multiple of 13.4x, while its current P/E is significantly lower than that of Toyota (16.26) and Honda (19.44) and slightly below General Motors ([GM], 13.43). However, on a 12-month forward P/E Hyundai looks extremely attractive and is trading at a cheap 6.70x vs the peer group average of 9.68x.
- In our view, Hyundai offers investors a quality share with compelling valuations. The company has grown significantly over the past decade and is still growing strong with the best profitability among its peers. Although it may be impacted in the short-term by labour unrest and currency fluctuations, Hyundai has plans in place to deal with these issues and we believe the share provides good long-term value for the serious investor.

Hyundai's forecasts are as follows:

Hyundai				
December y/e	**FY12**	**FY13E**	**FY14E**	**FY15E**
EPS (KRW)	31 515	35 103	38 978	39 493
% growth		*11%*	*11%*	*1%*
DPS (KRW)	1 900	1 946	2 017	2 162
P/E	8.1x	7.2x	6.5x	6.4x
DY	0.7%	0.8%	0.8%	0.9%
Share price (KRW)	**254 000**			
12-mnth fwd P/E	6.7x			

Source: Bloomberg, Anchor Capital

Global Ideas is a newsletter published three times a week (Monday, Wednesday and Friday) and available only to clients of Investor Campus and Anchor Capital. The key objective of this newsletter is to provide ideas for investment in the global investment universe.

We scan the globe looking for good opportunities. We provide our model portfolios, as well as news and views on our watch-list, which is continually reviewed and updated.

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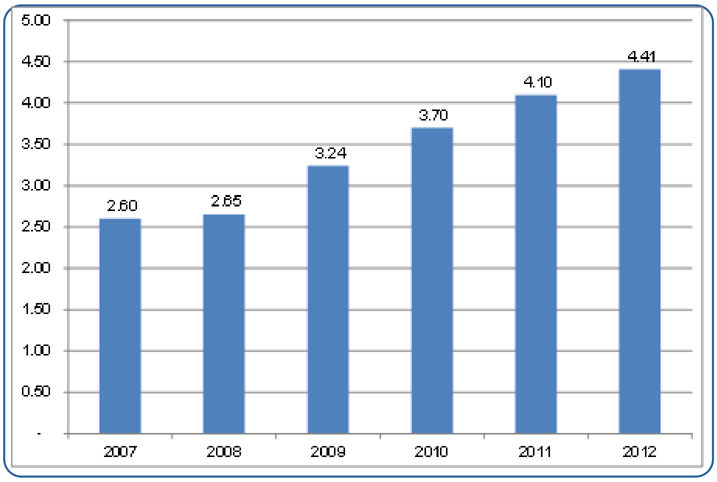
What it does:

Hyundai, along with Kia Motors (a c. 34%-owned subsidiary), comprise the Hyundai Motor Group. The company is a South Korean manufacturer, seller and exporter of passenger cars, trucks and commercial vehicles. It also sells auto parts, operates auto repair service centres and provides financial services through its more than two-dozen auto-related subsidiaries and affiliates. Hyundai consists of three business divisions (vehicle, financial and other business) which collectively exist in a synergistic relationship with each other. For example, Hyundai Steel (part of the other business division) develops and produces lightweight, highly malleable steel which is designed for cars. This enables Hyundai Motor to apply its quality management process from the initial raw-material stage. It is also a major supplier of construction steel in South Korea, with its financial division (10% of sales) providing automobile financing and credit card services. Hyundai's vehicle division manufactures passenger cars (including the Centennial, Genesis, Veloster, Azera, Sonata, i40, Elantra etc.), sport utility vehicles (SUVs) and commercial vehicles (trucks, buses, special vehicles and bare chassis) and accounts for c. 84% of sales. The company also provides automobile maintenance services and related components.

Background:

Hyundai was founded in 1967 and is now the fifth-biggest vehicle manufacturer globally based on 2012 annual vehicle sales. In terms of size Hyundai has c. 75,000 employees and last year it (together with its Kia affiliate) sold 4.4mn vehicles globally (+8.6% vs 2011). This despite the extremely competitive global automobile market and the crisis in Europe. Hyundai vehicles are currently sold in 193 countries through c. 6,000 dealerships and showrooms.

Hyundai global sales, 2007-2012 (mn units):



Source: Company reports, Anchor Capital

The group is currently ranked 89th on the *Forbes* Global 2000 list and it comes in 95th position in sales, 57th in profit, 224th in assets and 206th in terms of market value. In 2012, the Hyundai brand attained 53rd (7th among car companies) position out of the top-100 global brands (as surveyed by *Interbrand*) reflecting a 24% increase in its brand value to $7.5bn from the previous year. Hyundai has production facilities across the globe. In South Korea it has three: Ulsan, the largest in the world with an annual capacity of 1.55mn units, the Asan facility, which produces around 300,000 mid- and large-sized cars p.a. (for export), and its Jeonju factory which, with a capacity of 100,000 p.a., is the world's largest production centre for commercial vehicles. Hyundai also has facilities in the US, China, India, the Czech Republic, Turkey, Brazil and Russia.

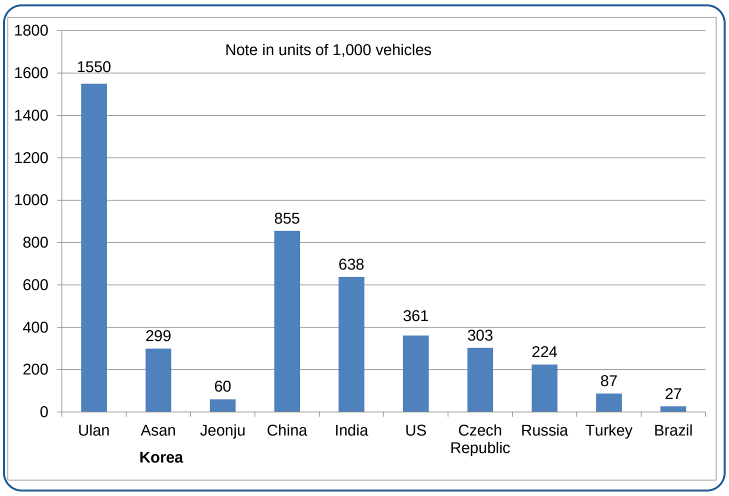
Hyundai sales FY12 vs FY11:

		FY11	FY12	YoY % change
Domestic sales	Passenger cars	421 696	393 707	-6.6
	SUVs	76 814	112 007	45.8
	CVs	185 060	162 063	-12.4
	Total	**683 570**	**667 777**	-2.3
Overseas sales	Exports	1 193 343	1 235 071	3.5
	Overseas plants	2 174 803	2 499 099	14.9
	Total	**3 368 146**	**3 734 170**	10.9
	Global sales total	*4 051 716*	*4 401 947*	8.6

Source: Company reports, Anchor Capital

1. *Commercial Vehicles (CVs) include buses and trucks*
2. *Hyundai Motor currently has seven overseas plants in Brazil, China, the Czech Republic, India, Russia, Turkey and US*
3. *excludes CKD (Complete Knock Down) unit sales*
4. *unit=1 vehicle*

Hyundai factories and production, 2012



Source: Company reports, Anchor Capital

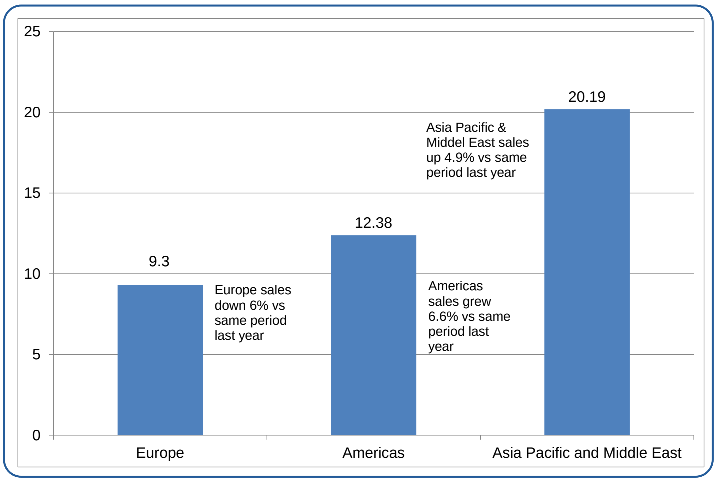
Growth drivers:

The following are what we believe to be the key growth drivers for Hyundai going forward:

- **Growing global vehicles sales:** According to the *International Organisation of Motor Vehicle Manufacturers (OICA)* in 2012 world vehicle production reached a record 84.1mn (all types), up more than 5% compared with 2011, while global sales figures (all vehicle types) were estimated at c. 82mn vehicles last year. Recently the *OICA* said that in the first six months of this year, globally new vehicle registrations rose 2.8% to 42.64mn units. This was on the back of booming demand from emerging markets (EM) which the organisation said was driving up global sales of new vehicles, thereby making up for declining sales in Europe. Mature markets now only represent 47% of global sales. In terms of passenger cars alone, global sales grew 1.9% to 31.46mn in 1H13.

In the US vehicle sales rose 7.3% to 7.96mn for 1H13 with that country's auto industry experiencing a boom and analysts forecasting that vehicle sales next year will reach over 16mn units (marking five consecutive years of growth). In China vehicle sales remain robust and in 1H13 *OICA* data show new vehicle sales jumped 12.3% to 10.78mn. All of this is good news for Hyundai. The company has a global presence, is strong in the US and especially in China and even in Europe where vehicle sales are falling, Hyundai experienced growth, having grown its market share in the region from 2.9% in 2011 to 3.5% in 2012. In contrast competitors such as Toyota and VW were unable to grow their operations in Europe.

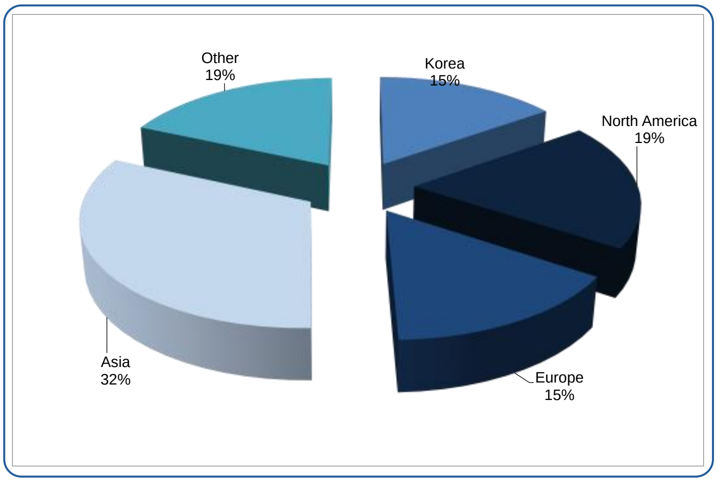
New vehicle sales by region, mn (1H13)



Source: OICA, Anchor Capital

- **Asia:** Hyundai is ideally located in the buoyant Asian region which already accounts for c. 47% (including Korea) of their sales. Although the west is important (*see our comment on the US below*), by comparison North America and Europe represented only 19% and 15% of sales, respectively, in FY12.

Hyundai retail sales by region, FY12



Source: Company reports, Anchor Capital

The International Monetary Fund's (IMF) GDP growth forecasts for developing Asian countries including China, India and five of the Association of Southeast Asian Nations [ASEAN] countries (Indonesia, Malaysia, Philippines, Thailand, and Vietnam) are the highest of any region in 2013 and 2014. Economic expansion rates at these levels are a promising indication of wealth creation which will fuel new car demand growth.

IMF Asia GDP forecasts:

	2013	2014
Developing Asia	*6.9*	*7.0*
China	7.8	7.7
India	5.6	6.3
ASEAN-5*	5.6	5.7

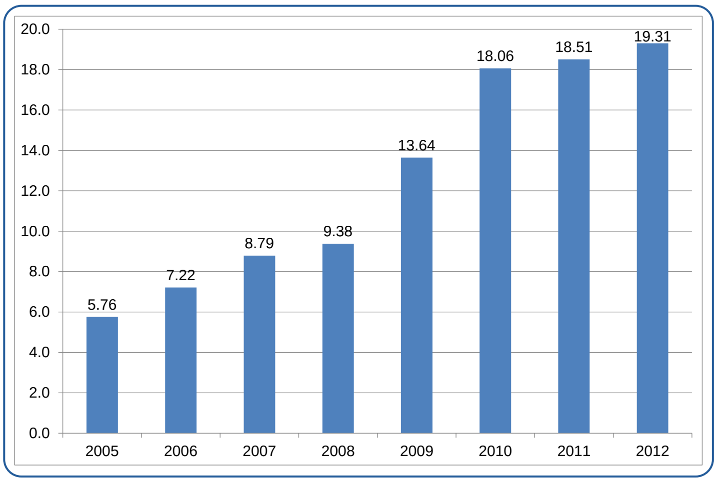
Source: IMF

** Indonesia, Malaysia, Philippines, Thailand, Vietnam.*

- **China:** In January 2009, China became the world's largest automobile market by vehicle sales and according to the *China Association of Automobile Manufacturers*, 1.6mn vehicles were sold in China last month, up 10.3% YoY. Between January and August, 13.95mn vehicles were sold - up 11.8% from the same period last year. From these numbers it's clear that China is, metaphorically speaking, the golden goose for vehicle manufacturers. A recent *PriceWaterhouseCoopers (PWC)* report says that the global auto market will continue to expand in the coming years, driven by China where sales are expected to nearly double by 2019. Thus, despite concerns around China's slowing growth, it remains the biggest market for Hyundai, with the company continuing to expand its presence in the country and recently starting operations at its third China plant, establishing a system to produce and sell 1mn vehicles p.a. in China.

  In July Hyundai said that since debuting in China a decade ago its cumulative car sales there have exceeded the 7mn mark and in early September it reported sales of 1mnn units in China YTD -- the fastest pace since it entered that market. This rapid growth is in large part due to Hyundai's new models including the K3 and on the back of China's burgeoning SUV market which boosted sales of the Hyundai Tucson by as much as 75%. No matter which way you look at it, China is a huge (and the most important) market for Hyundai. The company is all too aware of this, saying recently that the Chinese market has become the focus of its sales target. The fact that Hyundai already has a significant presence there can only help stimulate its already impressive growth. To get an idea of the growth potential in China one need only look at the motorisation rate (the number of cars per 1,000 inhabitants) data from the *OICA*. The motorisation rate is lowest in Africa (41 per 1,000 inhabitants) while in the US, Canada and Mexico, there are 644 cars per 1,000. Importantly, China's motorisation rate is also extremely low at only 68 cars per 1,000, however it is also growing extremely fast thus offering an extraordinary opportunity for Hyundai to benefit.

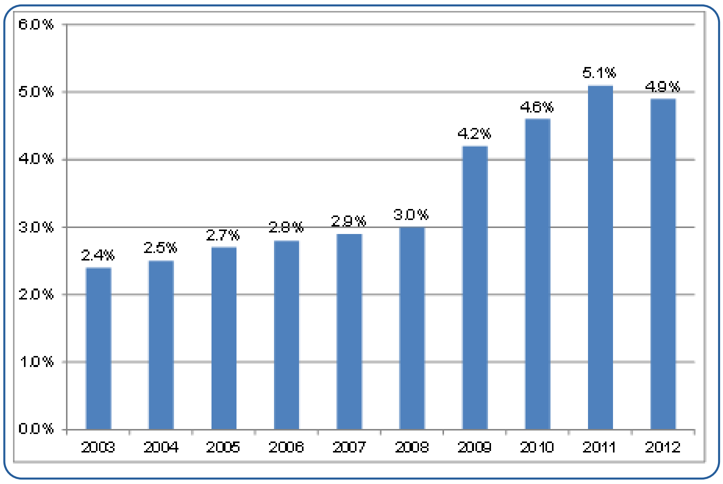
China all vehicle sales, 2005-2012 (mn)



Source: OICA, Anchor Capital

- **US:** The US economy is turning around and new car sales are improving dramatically. Overall automakers sold 14.8mn light vehicles in the US market last year, up 13% from 2011, and the highest level since 2007. 2012 also marked the third-straight year of at least a 10% increase in sales. With the average age of US cars still at a record-high of 11.4 years, and increased consumer confidence it follows that US consumers will be taking advantage of the still-low interest rate environment and will be buying cars to replace so-called clunkers with new models. The strong momentum in the US auto market also gives automakers better pricing power and Hyundai is currently extremely popular. Last year the company's facility in Alabama set an annual production record of 361,348 units, but this was not enough to satisfy the robust demand (which in the end cost the company market share). Although Hyundai's US market share has been steadily growing over the past ten years (with a slight hiccup last year due to the lack of stock), it currently still only stands at c. 4.9%.

Hyundai US market share, 2003-2012:

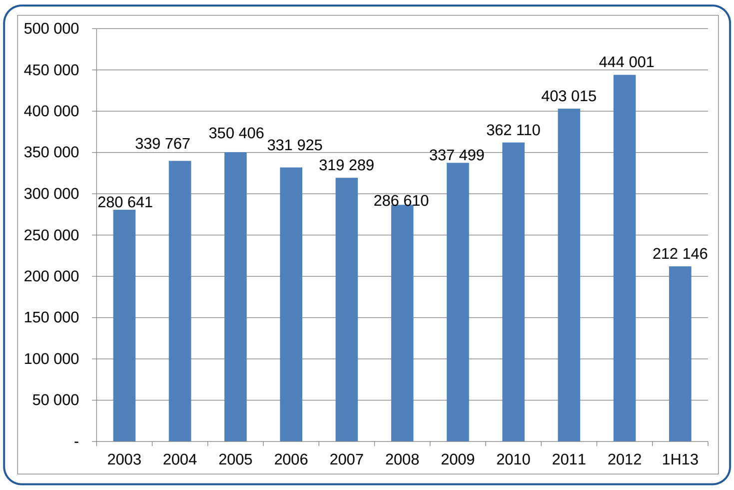


Source: Company reports, Anchor Capital

However, we highlight that capacity constraint in the US in 2012 impacted Hyundai resulting in a slower pace of growth than the industry. Although some might interpret this as being a good problem to have the company will need to address this issue. Press reports have suggested Hyundai will be building other plants in the US, but no plans have been confirmed by the company. In the interim Hyundai has promised to enhance its customer service there and to continue to draw customers to the brand .

- **Other territories:** Globally, Hyundai has said it expects to boost sales in Brazil (and China), where there are new plants with even greater capacity. The newly inaugurated plant in Brazil, basically secures production bases for Hyundai in all the major markets around the world. The company has also indicated it will reinforce the sale of luxury cars in the Middle East and Russia. In FY12 as a result of the European debt crisis, car sales in the region were disappointing, while growth momentum in EMs was further diminished. For the first time since 2008, the Korean domestic market also recorded negative growth, on the back of an increase in household debt and a decline in consumption. Despite this Hyundai continued to grow last year, selling 4.4mn units or 120,000 units more than its 4.29mn unit business target. Japanese demand for cars is also expected to normalise in 2013 after sales rebounded last year following the slowdown caused by the 2011 tsunami and earthquake. *Moody's* estimates a normalised level to be around 4.7mn units and expects demand in CY13 to fall by 11% to 4.7mn units and broadly remain at that level in 2014 (up 1% to around 4.75mn). According to the latest *Scotiabank Global Auto Report*, throughout North America, purchases are moving steadily higher with passenger vehicle sales (cars and light trucks) in Canada on target to climb to a record high in 2013. The sales trend has started to stabilise in Western Europe (the third-largest auto market) while the Brazilian market was a source of strength earlier this year as car sales climbed to record highs through May.

Hyundai Western Europe vehicle sales, 2003-1H13:



Source: Company reports, Anchor Capital

- **A rapidly growing reputation and brand value:** China's auto industry has an estimated 100 companies, many of which are niche players with ties to global groups, making everything from passenger cars to buses. However, as the average Chinese middle-class consumer aspires to move higher up the economic ladder, established brands such as Hyundai, GM, VW etc. are leveraging their status as quality vehicle manufacturers in order to get a jump on domestic rivals, which mostly target the lower-priced segment of the market. Globally we believe the public's perception of the Hyundai brand has been transformed significantly over the past decade or so as a result of dramatic improvements in the quality of the company's vehicles. This is borne out by the findings of brand consultancy firm *Interbrand* which has included Hyundai in the Best 100 Global Brands list for eight consecutive years and, compared with its position in 2005, Hyundai has grown faster than any other automotive brand. Last year the company saw its brand value surge 24.4% YoY to $7.5bn in *Interbrand's 2012 Best 100 Global Brands survey*. According to the study, Hyundai's increasing popularity is shaped by its expanding model line-up, as well as perceptions of the brand's quality and appeal improving over the past 10 years. Following on from this another positive is the variety of vehicles Hyundai produces. The company offers all types of vehicles from city cars to SUVs and sedans and at the same time it runs a tight ship and has streamlined its business model. Hyundai also provides competitive pricing and an attractive product with most of their cars having been redesigned by former Audi/VW design expert Peter Schreyer. This has enabled the company to gain market share over the past few years from other players in some of their key markets. In 2H12 for example, Hyundai and its associate Kia were the only brands gaining pace in Europe (+12% and +24%, respectively) while the German, French, US and Japanese manufacturers were impacted by a decline in demand ranging from -1% (BMW) to -17% (Fiat and Renault).

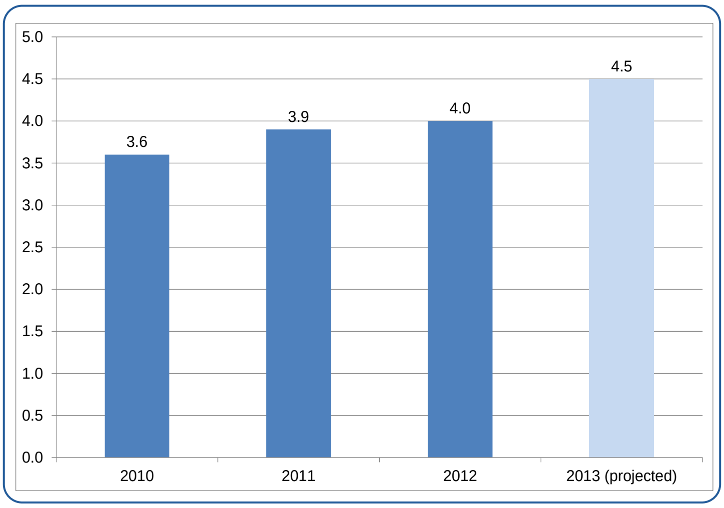
Hyundai brand value and ranking, 2005-2012

	Brand value ($bn)	Ranking within Top-100
2005	3.5	84
2006	4.1	75
2007	4.5	72
2008	4.9	72
2009	4.6	69
2010	5.0	65
2011	6.0	61
2012	7.5	53

Source: Interbrand, Anchor Capital

- **A focus on research and development (R&D):** Hyundai has R&D facilities in six different locations around the world (three in Korea and one in Germany, Japan and India). The company also has smaller R&D offices globally for example its design centre in California which develops designs specifically for the US market. Hyundai has also invested in manufacturing plants in North America, India, the Czech Republic, Pakistan, China and Turkey and is continuously financing R&D in areas such as eco-friendly vehicles in order for it to secure technological competitiveness. In its FY12 annual report Hyundai undertook to increase investment in R&D in the field of eco-friendly cars and electronic controls, while at the same time increasing its focus on nurturing talent to build technological competitiveness and advancements. All of these measures have yielded positive results for the company with Hyundai becoming a leader in the production of quality, dependable, safe (and eco-friendly) cars.

Hyundai R&D spending, 2010-2013



Source: Interbrand, Anchor Capital

- **The rising cost of fuel and environmental factors:** As mentioned above Hyundai is continuously investing in the development of eco-friendly vehicles by making headway with so-called green cars through hybrid and fuel-cell electric technologies. Although currently this represents only a small percentage of the company's sales, in the future it has the potential to grow enormously. Its Blue Drive strategy has seen green technology spearheading the development of low -pollution, highly fuel-efficient cars. With fuel prices increasing significantly this should open up markets for the company's hybrid, electric and hydrogen-fuelled cars as consumers look for cheaper alternatives. People are also becoming more environmentally conscious (especially in developed markets) and will likely choose more fuel-efficient hybrid, electrical or hydrogen-fuelled cars which Hyundai offers. Zero CO2 emissions is a target to which most car companies aspire but Hyundai has come a step closer with its Blue Drive strategy which aims to improve the fuel economy of mass production models and to develop a variety of new eco-friendly vehicles.
- **Profitability:** Hyundai's FY12 operating margin is close to 10% - the highest amongst its competitors with the exception of premium vehicle manufacturer BMW (at c. 10.9%). Hyundai has indicated that its strategy is to improve on this number by shifting to a more profitable product mix which leans towards mid-and large-size sedans and SUVs and by lowering incentives and marketing costs and promoting the sale of compact cars, which are popular with customers even in times of an economic downturn.

The high profitability is explained partly by Hyundai's higher than average capacity utilisation and its low inventory levels (whereas its European peers in most cases are hurt by overcapacity). It follows therefore that because of its low inventory levels, there is less need to mark down vehicle prices in order to lift sales, leading to high structural operating margins. Also, Hyundai's own steel division is a major supplier allowing the company to have lower costs than most in the peer group. It should be noted though that in terms of RoE, in FY12 Hyundai's was 16.4% which was slightly below the average RoE (18.5%) of the peer group (excl. Hyundai) and below that of Ford (which was the highest at 36.6%), VW (at 32.2%), BMW (17.8%) and GM (17.1%). However it was above that of Toyota, Honda and Nissan.

Hyundai operating margin and RoE vs peer group

	RoE	Operating margin
BMW	17.8	10.9
Hyundai	16.4	9.99
Toyota*	8.5	5.99
VW	32.2	5.97
Honda*	7.8	5.52
Nissan	9.8	5.11
Ford	36.6	4.68
GM	17.1	3.14

Source: Marketwatch, Bloomberg, Thomson Reuters, Google Finance Anchor Capital

** indicates FY13*

Risks:

Below we highlight possible risk factors facing Hyundai:

- **Currency fluctuations:** Given its global footprint, Hyundai earns more than 50% of its revenue outside South Korea (it also sells 87% of its vehicles abroad and ships auto parts to its facilities globally). This means the company is naturally exposed to exchange rate fluctuations which can have an impact on its sales, earnings and cash flows. Thus if the Korean won appreciates against other currencies, for example the dollar, it will negatively impact Hyundai's turnover. With the won appreciating c. 2.8% YoY vs the dollar (on average) in 2Q13 and by 1.5% YoY thus far in 3Q13 (up to 17 September), it will have reduced the value of Hyundai's repatriated foreign earnings. If Japan weakens the yen (which the government there has done and indicated it will still do) to support the domestic economy this also has an impact on Hyundai's earnings in that country. A weaker yen makes vehicles built in Japan more price competitive abroad and is positive for Japanese companies such as Honda or Toyota. A Hyundai executive recently called the simultaneous yen decline and won increase "a double-torture situation".

Korean won vs US dollar:

	4Q11	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13	3Q13
	1 144.1	1 129.5	1 148.9	1 128.9	1 085.6	1 079.1	1 117.3	1 111.9
QoQ	6.0	-1.3	1.7	-1.7	-3.8	-0.6	3.5	-0.5
YoY		1.1	6.2	4.6	-5.1	-4.5	-2.8	-1.5

Source: Oanda, Anchor Capital

Red indicates strengthening of the Korean won vs dollar

- **The impact of labour disputes.** South Korea has a history of volatile domestic labour relations and according to data compiled by the country's *Ministry of Employment and Labour* the number of work days lost on labour disputes more than doubled to 933 days in 2012 (from 429 in 2011). Analysts have frequently cited labour unrest by Hyundai's union, which is particularly militant, as one of the biggest threats to the company's earnings. This year Hyundai faced a number of strikes over pay disputes which impacted sales and earnings. For six weeks in March/April, 45,000 unionised employees refused to work during weekends, hurting both the company's domestic shipments and its exports to other markets (especially the US) from its biggest manufacturing base. On top of that the company estimates total production lost through partial strikes in August at 21,392 vehicles or KRW438.3bn ($394mn). Hyundai has said it expects to be able to recoup the losses by increasing production over the remainder of 2013 but concerns remain that the union will stage further strikes. Although Hyundai has steadily been increasing its overseas production, by opening new factories in places like China and Brazil, nearly half its output still comes from its South Korea factories, which the company has also said suffers from lower productivity relative to their high labour costs vs other countries such as the US.
- **Intensifying competition**: In some of its crucial markets, Hyundai has been struggling to defend its market share amid intense competition. For example Hyundai has said it expects competition with Japanese automakers to increase as they step up and/or continue incentives and discounts on the back of the weaker yen. Some of Hyundai's models (such as Sonata and Elantra) are also ageing resulting in Hyundai having to cut the prices on these vehicle or giving customers more incentives from a year ago to lure them from rivals and trigger consumer demand for its ageing models. This year EMs such as China and India also saw Japanese and American automakers stepping up their game and presenting fierce competition for Hyundai in these markets. The result of this is that Hyundai has to compete on price which will likely impact the company's profit.
- **Negative publicity and product recalls:** Hyundai has had to recall literally millions of cars over the past four years because of several faulty car parts. In April this year Hyundai (and its Kia subsidiary) said they were recalling almost 1.9mn vehicles to fix problems with air bags and brake light switches and in August the company announced it would recall 259,000 automobiles affecting four different vehicle models. Although almost every vehicle manufacturer has had to recall faulty products (see tables below) it nevertheless creates significant bad publicity and has an impact on the reputation of the manufacturer.

At the same time it also erodes any competitive advantage the company has worked for years to build. In the US Hyundai was also accused of falsifying gas mileage estimates on its cars. This has resulted in the business facing federal as well as class action lawsuits to reimburse damage done to customers.

Biggest vehicle recalls in US history, mn:

	Year	Number of vehicles (mn)
Ford	2009	14.0
Ford	1996	7.9
Toyota	2012	7.4
GM	1971	6.7
Toyota	2010	6.7
GM	1981	5.8
Ford	1972	4.1
GM	1973	3.7
GM	2004	3.7
Honda	1995	3.7
VW	1972	3.7

Source: wmur.com

Biggest US auto recalls, 2012:

Honda	2 806 762
Toyota	3 948 000
Chrysler	744 822
Ford	485 000
GM	426 240

Source: Forbes, Anchor Capital

- **Japan:** Japan represents a significant automotive market and performing poorly there definitely leaves Hyundai at competitive disadvantage. The aggressive monetary policy by the Bank of Japan (BoJ) which has massively weakened the yen and favoured Japanese car producers like Toyota and Honda has impacted Hyundai. This trend has already caused a big drop in its 4Q profit and could still go on for a while. Japanese exporters are also benefiting the country's economic policies, which have helped drive down the yen since late last year, and assisted automakers in absorbing slowing sales in China (due to a territorial dispute between China and Japan). Analysts estimate the Japanese currency, which saw Nissan cut car prices in the US., will probably weaken further this year. While the yen weakens (positive for Japanese automakers) the Korean won is appreciating (negative for Hyundai).

Results:

Hyundai released FY12 results in January which showed revenue had risen 8.4% YoY to $75.6bn, while operating income came in at c. $7.55bn and operating profit was $7.89bn (up 5.1% YoY) fuelled by a robust performance at its overseas plants and subsidiaries. Despite the challenging business environment with fluctuating exchange rates, Hyundai managed to sustain its upward momentum selling 4,410,357 units globally - an 8.6% YoY increase. Although the company's sales in Korea fell 2.2% to 667,496 units, overseas sales rose 10.8% to 3,742,861 units. Also positive was the news that the company's sales jumped over 10% in Europe to 444,000 units, bucking the trend there of shrinking demand amid the debt crisis in the region. To overcome sluggish demand in the Korean domestic market, Hyundai aggressively expanded its exports from Korea, while at the same time boosting sales in overseas markets through its local production and sales network. The company said it aims to sell 4.66mn vehicles globally in 2013 (668,000 in Korea and nearly 4mn overseas), an 5.7% YoY increase.

During 1H13, Hyundai was able to maintain its growth path despite the weak auto markets (especially in Europe), increasing sales by 5.8% YoY to $40bn. However once again the company was exposed to currency risk (due to currency movements vs its reporting currency [the South Korean won]) which, despite Hyundai attempting to mitigate these risks by way of hedging, settlement currency diversification and reduced exports from Korea, still had an impact.

Hyundai vs peer group

Relative to Ford, Nissan, BMW and VW, Hyundai is trading at higher current P/E multiple of 13.4x, while its current P/E is significantly lower than that of Toyota (16.26) and Honda (19.44) and slightly below General Motors ([GM], 13.43). However, on a 12-month forward P/E Hyundai looks extremely attractive and is trading at a cheap 6.70x vs the peer group average of 9.68x.

Hyundai vs peer group:

	Current P/E	12M fwd P/E	DY	12M fwd DY	P/Book
GM	13.43	9.65	na	0.12	1.88
Nissan	11.84	8.35	2.51	3.01	1.10
Toyota	16.26	11.22	1.42	2.49	1.57
BMW	10.13	10.10	3.13	3.32	1.66
VW	4.78	7.50	2.05	2.31	1.01
Honda	19.44	10.01	1.99	2.28	1.32
Ford	11.44	10.95	2.30	2.27	3.65
Peer avg (excl. Hyundai)	**12.47**	**9.68**	**2.23**	**2.26**	**1.74**
Hyundai	***13.40***	***6.70***	***0.75***	***0.77***	***1.36***

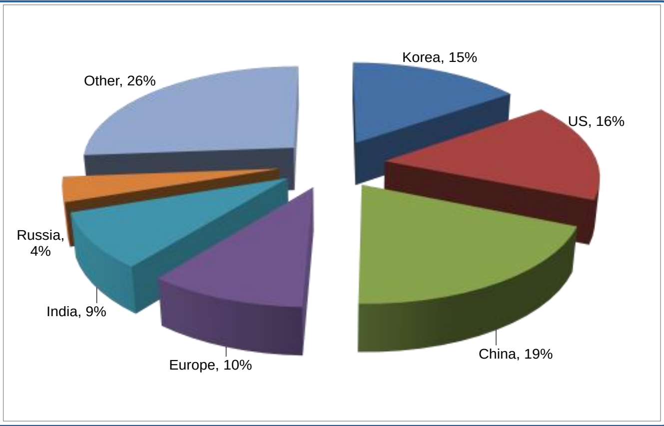
Source: Bloomberg, Company reports, Anchor Capital

Conclusion:

Hyundai has been one of the world's fastest-growing auto makers in recent years with above average sales growth over the past five years of c. 7% p.a. It has also grown its reputation with most people now identifying the brand with quality and excellent service (quite a turnaround from its image in the late 1990s). The company is also competing on a global scale with the world's biggest automobile manufacturers. Hyundai has addressed further expansion opportunities with manufacturing facilities and production bases strategically located in all major markets across the globe. Last year it opened its first manufacturing plant in Brazil and the company also started operations at its third plant in China, thus establishing a system to produce and sell one million vehicles in Brazil p.a.

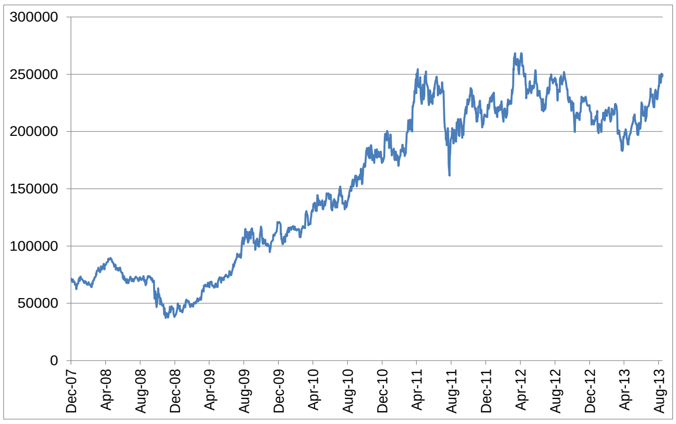
Its Russia factory is the fastest-growing car plant in that country, starting operations in January 2011 with an annual production capacity of 150,000 units which has now increased to 200,000 units in order to meet the demand. The US market is also set to continue on a growth path (US new car sales reached a six-year high in August) after recording double-digit growth each year for the past three years. In August, Hyundai set another sales record in the US despite the impact of capacity problems which were worsened by a labour dispute in South Korea. US sales are growing quickly at c. 20% p.a. but it should be noted here that if US capacity constraints continue, the company may not fully benefit from the growth in the US vehicle market. This year has also seen sales in China (its biggest market) picking up speed. All of the above bodes well for Hyundai's continued success and growth. Although Europe will likely remain sluggish for a little while longer (due to the debt crisis), it too is showing signs of a recovery and with Hyundai posting increases in its market share in the region during the recession, once a turnaround happens it can only spell good news for the company. The fact that Hyundai's has a globally diversified business is extremely positive for the growth of the company.

Hyundai sales by market:



Source: Company data, Anchor Capital

Hyundai share price performance, 2008 to date (KRW):



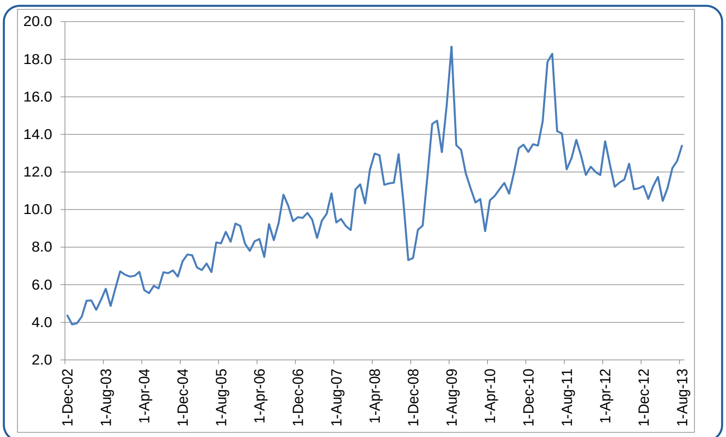
Source: Bloomberg, Anchor Capital

Looking at the share price, Hyundai has done extraordinarily well for its shareholders since the financial crisis with the share price up nearly 550% since its 2008 low of KRW37100/share on 25 November 2008. The share price came under pressure during the company's costliest ever work stoppage in July/August 2012 which halted production of more than 82,000 cars worth around $1.5bn. Since then it has come back by around 15% and YTD Hyundai's share price is up 16.2%.

Hyundai is an extremely profitable company, with an average operating margin of c. 10% (higher than any other auto maker except for BMW). The company keep its costs down, despite the recent appreciation of the Korean won, by sharing everything from design to manufacturing and sales through its divisions. Globally, Hyundai has the lowest inventory level of 3% while other top auto players such as BMW and GM are at 7.4% and 9.8%, respectively.

We believe Hyundai is good value compared with its global peers and, in addition to its attractive valuation, the company looks well-positioned to manage supportive market dynamics in its favour both at home and abroad. Hyundai is trading at a low 12-month forward P/E of 6.70x - the cheapest vs the global peer group average of 9.68x.

Hyundai historic P/E, December 2002 to date:



Source: Bloomberg, Anchor Capital

In our view Hyundai offers investors a quality share with compelling valuations, posting good sales growth and with the best profitability among the major global auto makers. Although it may be impacted in the short-term by labour disputes and currency fluctuations, Hyundai has plans in place to deal with these issues and we believe the share provides a good long-term value proposition for investors.

Hyundai's metrics are as follows:

Spot (KRW)	254 000
MKT Cap (KRWmn)	55 950 224
12M trailing P/E	13.40
12M fwd P/E	6.70
10-year average P/E	12.2
FYE	31-Dec
P/Book Ratio	1.36
12M fwd DY	0.77

Source: Bloomberg, Anchor Capital

Marco de Matos

The business of money: Global asset management and stockbroking

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