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CYD - Q2 2013 China Yuchai International Limited Earnings Conference Call and Webcast

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by and welcome to the China Yuchai International Limited Q2 2013 earnings conference call. At this time all participants are in a listen-only mode. There will be a presentation followed by a question and answer session. (Operator Instructions). I would now like to hand the conference over to Kevin Theiss. Please go ahead, sir.

Kevin Theiss - *Grayling - IR*

Thank you for joining us today and welcome to China Yuchai International Limited's second quarter and half year ended June 30, 2013 conference call and webcast. My name is Kevin Theiss and I am with Grayling, China Yuchai's US investor relations advisor. Joining us today are Mr. Weng Ming Hoh and Mr. Kok Ho Leong, President, and Chief Financial Officer of CYI respectively. In addition, Mr. Kelvin Lai, VP of Operations of CYI, is also joining us today.

Before we begin, I will remind all listeners that throughout this call, we may make statements that may contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The words "believe", "expect", "anticipate", "project", "targets", "optimistic", "intend", "aim", "will", or similar expressions are intended to identify forward-looking statements. All statements other than statements of historical fact are statements that may be deemed forward-looking statements. These forward-looking statements are based on current expectations or beliefs, including, but not limited to, the statements concerning the Company's operations, financial performance and condition. The Company cautions that these statements by their nature involve risks and uncertainties, and actual results may differ materially depending on a variety of important factors, including those discussed in the Company's reports filed with the Securities and Exchange Commission from time to time. The Company specifically disclaims any obligation to maintain or update the forward-looking information, whether of the nature contained in this conference call and release or otherwise, in the future.

Mr. Hoh will provide a brief overview and summary and then Mr. Leong will review the financial results for the second quarter and half year ended June 30, 2013. Thereafter, we will conduct a question and answer session. For the purposes of today's call, the financial results are unaudited and they will be presented in RMB and US dollars. All the financial information presented is reported using International Financial Reporting Standards as issued by the International Accounting Standards Board. Mr. Hoh, please start your presentation.

Weng Ming Hoh - *China Yuchai International Limited - President*

Thank you, Kevin.

We are pleased to report that we continued to grow in the second quarter of 2013 as our net revenue, operating profit and net profit exceeded the results of the second quarter in 2012. Net revenue rose 24.1% in the second quarter to RMB4.25 billion or US$688.1 million. Our total engine sales increased 29.1% year over year to 141,000 units, outpacing diesel-powered commercial vehicle industry sales, as reported by the China Association of Automobile Manufacturers "CAAM". We continued to expand our market share in the second quarter of 2013 as we maintained a leading position in the world's largest commercial vehicle market.

During the second quarter, truck unit sales in China increased 15.1% with growth mainly due to pre-buying of new trucks before the implementation of the National IV emission standards on July 1, 2013.

An important part of our growth strategy is to supply multiple engine solutions for diversified markets. To accomplish this, we continued to increase our investment in research and development "R&D". R&D expenses grew 21.6% to RMB115 million in the second quarter of 2013. We remain committed to the development of advanced, new engines to meet the evolving needs of our customers and capture new market share, as well as improve the performance and quality of our existing engines.

Through our R&D program, our customers now have the option of diesel, hybrid and natural gas engines for their vehicles. We expanded our natural gas models so that most of our diesel engines have a natural gas alternative to help our customers conserve fuel and reduce emissions where applicable. To capture further market share in the off-road construction, mining, marine, and power generation markets, we introduced new higher horsepower diesel and natural gas engines. The growing range and advanced performance of our engines provide us with sales opportunities that we can quickly respond to as market requirements change.

Although the National IV emission standards were implemented on July 1, 2013, we had in 2007 already started producing standard engines compliant with National IV and V emission standards far ahead of the requirement. Our range of advanced engines is one of the reasons why we have captured a leading market position in the important Chinese bus market, which requires lower emissions as most buses operate in the urban areas. The rapid expansion of our portfolio of natural gas engines, with their lower emissions and fuel conservation, solidified our dominance over the bus market.

Two recent examples of the effectiveness of our R&D efforts are --

- 16 of Guangxi Yuchai Machinery Company Limited's "GYMCL" engines have been awarded a CE safety certification. In the European Union, such certification is required before any products are allowed to be sold in the EU markets. This opens a potential new sales channel for us.

- At a recent session of the National Work Conference on Machinery Brand Strategy Advancement, a list of 101 advanced machinery brands in China was released and GYMCL's independently developed YC6-L diesel engine series for heavy-duty commercial vehicles was included on the list. The YC6L engine series has been awarded five patents for invention and 37 utility patents.

Our new Research and Development Institute located in the High-Tech Development Zone of Nanning, the capital of Guangxi Province, is expected to be operational by the end of 2013. The R&D Institute will enhance our capabilities to develop new engine designs and technologies to improve and diversify our range of engines.

The development of new production capacities for natural gas engines and high horsepower engines are on schedule. The natural gas facility is expected to be operational in the second half of 2013 to support the growing demand for our suite of compressed natural gas and liquid natural gas engines. In the first half of 2013, sales of our natural gas engines continued its upward trend as we sold approximately 13,000 natural gas engines, representing a significant increase in the first six months of 2013 compared with the same period a year ago.

Let me now provide an update of our joint ventures.

The market for heavy-duty engines remains attractive long term and sales of heavy-duty trucks in the second quarter of 2013 in China were up more than 30%. The YC6K engine provides strong performance with low emissions and we are using this next-generation design to build larger and more powerful engines. The YC6K-designed engines supplement our existing 6L, 6M, 6G and 6MK heavy-duty engines as we build our capabilities to become one of the largest heavy-duty engine manufacturers in China.

Our 'green' joint venture with Caterpillar is now fully operational remanufacturing engines and parts. Engine remanufacturing conserves raw materials and reduces pollution compared with manufacturing new engines and saves money for the customer. As with many new technologies, it will take time to build customer acceptance in China but our joint venture is at the forefront of introducing this cost-effective, emerging service to the marketplace. We continue to believe that the long-term outlook remains favorable.

Light-duty vehicles represent the largest segment of the commercial market in China. Our joint venture with Geely continues to test the second generation of the 4D20 diesel engines for use in passenger cars and light-duty commercial vehicles. Testing is expected to be completed by the end of 2013.

On June 4, 2013 we announced the entry into a framework agreement for the establishment of a new joint venture between GYMCL and its subsidiary Y&C Engine Company, and Baotou Bei Ben Heavy Duty Truck Co., Ltd. and Inner Mongolia First Machinery Group Co., Ltd. New advanced diesel and gas engines will be designed and produced for Bei Ben's heavy-duty and medium-duty trucks and buses. Bei Ben is a leading truck manufacturer in China.

We continue to be the leader in the commercial engine market as we sold 271,000 engines in the first half of 2013, a 12.8% increase over last year's first half. With 12 new engines to be introduced during 2013 and new production capabilities coming on-stream, we are prepared to capture market share in both on-road and off-road markets.

For the second quarter of 2013, we generated positive cash flows from operating activities and invested in property, plant and equipment. We believe in continually investing our cash flow to build our operations and provide a return to our shareholders.

To reward our shareholders, we declared on June 17, 2013 a cash dividend of US$0.40 per ordinary share and a special cash dividend of US$0.40 per ordinary share for the year ended December 31, 2012. The cash dividend was paid on July 10. Additionally, we have today, also announced that the Board of Directors has approved the payment of an interim dividend of US$0.10 per ordinary share to be paid on August 26 to shareholders of record as of the close of business on August 16, 2013. We believe that the payment of cash dividends is the best way to share our operational success with all our shareholders.

Entering into the second half of 2013, we remain cautious due to the uncertainty of the Chinese economy. However, we stay focused on building stronger relationships with our OEM customers, expanding our margin share and generating a steady cash flow.

With that, let me now turn the call over to Kok Ho Leong, our CFO, to provide more details on the financial results.

Kok Ho Leong - *China Yuchai International Limited - CFO*

Thank you, Weng Ming.

Let me first walk you through our unaudited second quarter and first half ended June 30, 2013 financial results and then we can begin the Q&A session.

Net revenue for the second quarter of 2013 was RMB4.25 billion, US$688.1 million, compared with RMB3.43 billion in the second quarter of 2012. The increase in net sales was RMB825.5 million or 24.1% as compared with the same period in 2012.

The total number of engines sold during the second quarter of 2013 was 141,147 units compared with 109,329 units in the same quarter a year ago, representing an increase of 31,818 units, or 29.1%. This was mainly attributable to an increase in the sales of engines for agriculture and truck applications. The increase in the sales of commercial vehicles was mainly due to the pre-buying of trucks prior to the implementation of the National IV emission standards nationwide on July 1, 2013.

Gross profit was RMB855.2 million, US$138.4 million, compared with RMB674.1 million in the second quarter of 2012. Gross margin was 20.1% in the second quarter of 2013 compared with 19.7% in the second quarter of 2012. A higher volume of engines were sold in the second quarter of 2013 compared with the same period a year ago which enabled us to improve our gross margin.

Other operating income was RMB36.6 million, US$5.9 million, an increase of RMB25 million from RMB11.6 million in the second quarter of 2012. The increase in income was mainly due to lower foreign exchange losses in the second quarter of 2013 compared with the same quarter last year.

Research and development "R&D", expenses were RMB115.9 million, US$18.8 million, compared with RMB95.3 million in the second quarter of 2012, an increase of 21.6%. As a percentage of net revenue, R&D spending declined to 2.7% compared with 2.8% in the second quarter of 2012. The lower percentage was due to higher net revenues in the second quarter of 2013 compared with the same quarter in 2012.

Selling, general & administrative "SG&A", expenses were RMB442.1 million, US$71.6 million, up from RMB380.4 million in the second quarter of 2012, an increase of RMB61.7 million, or 16.2%. SG&A expenses represented 10.4% of net revenue in the second quarter of 2013 compared with 11.1% in the same quarter a year ago. The decrease was mainly due to higher sales volume in the second quarter of 2013 compared with the same quarter in 2012.

Operating profit increased by 58.9% to RMB333.8 million, US$54.0 million, from RMB210.1 million in the second quarter of 2012, mainly due to higher gross profit and other income, partially offset by higher R&D and SG&A expenses. The operating margin was 7.8% compared with 6.1% in the second quarter of 2012.

Finance costs declined to RMB39.6 million, US$6.4 million, from RMB62.2 million in the second quarter of 2012, a decrease of RMB22.6 million or 36.3%. The decrease was due to less bills discounting as well as lower interest costs relating to GYMCL's outstanding short-term financing bonds, "STFB", and medium-term notes, "MTN", compared with higher interest rates applicable to the outstanding STFBs in the second quarter in 2012.

The share of joint ventures was a loss of RMB10.0 million, US$1.6 million, compared with a loss of RMB6.2 million in the second quarter of 2012.

In the second quarter of 2013, total net profit attributable to China Yuchai's shareholders was RMB166.3 million, US$26.9 million, or earnings per share of RMB4.46, US$0.72, compared with RMB67.1 million or earnings per share of RMB1.80 in the same quarter in 2012.

May I now move on to the financial highlights for the six months ended June 30, 2013.

For the six months ended June 30, 2013, net revenue was RMB8.10 billion, US$1.31 billion, compared with RMB7.11 billion in the same period last year. The increase in net sales was RMB987.2 million, or 13.9%, as compared with the same six-month period in 2012.

The total number of diesel engines sold by GYMCL during the first six months of 2013 was 271,891 units compared with 241,026 units in the same period last year, representing an increase of 30,865 units or 12.8%. This increase was mainly attributable to an increase in the sales of engines for agriculture and truck applications in the second quarter of 2013. The increase in sales of commercial vehicles was mainly due to the pre-buying of trucks prior to the implementation of the National IV emission standards nationwide on July 1, 2013.

Gross profit was RMB1.63 billion, US$264.2 million, compared with RMB1.45 billion in the same period last year. Gross profit margin decreased to 20.2% in the first six months of 2013 as compared with 20.4% a year ago. This was mainly attributable to a shift in the sales mix to more light-duty engines as well as engines for agriculture applications with lower gross margins.

Other operating income was RMB57.5 million, US$9.3 million, an increase of RMB19.8 million from RMB37.7 million in the same period last year. This increase was mainly due to a smaller loss relating to the disposal of plant and equipment as compared with the same six-month period in 2012.

Research and development, "R&D", expenses were RMB210.7 million, US$34.1 million, compared with RMB177.2 million in the same period in 2012, an increase of 19.0%. As a percentage of net revenue, R&D spending rose to 2.6% compared with 2.5% in the same period last year. The R&D

expenses mainly related to the ongoing development of new and existing engine products as well as continued initiatives to improve engine quality.

Selling, general & administrative, "SG&A", expenses were RMB806.6 million, US$130.5 million, up from RMB756.7 million in the same period last year, an increase of RMB49.9 million or 6.6%. SG&A expenses represented 10.0% of net revenue for the first six months of 2013, compared with 10.6% in the same period last year. The decrease in the SG&A percentage was mainly due to higher sales in the first six months of 2013 as compared with the same period in 2012.

Operating profit increased to RMB672.7 million, US$108.9 million, from RMB557.3 million in the same period last year, mainly due to an increase in the gross profit and other income, partially offset by higher R&D and SG&A expenses. The operating margin was 8.3% compared with 7.8% in the same period last year.

Finance costs declined to RMB73.8 million, US$11.9 million, from RMB137.5 million in the same period last year, a decrease of RMB63.7 million, or 46.3%. The decrease was due to less bills discounting and lower interest costs relating to the outstanding STFBs and MTNs.

The share of joint ventures was a loss of RMB25.7 million, US$4.2 million, compared with a loss of RMB22.9 million in the same period last year.

For the six months ended June 30, 2013, total net profit attributable to China Yuchai's shareholders was RMB339.8 million, US$55 million for earnings per share of RMB9.12, US$1.48, compared with RMB235 million, or earnings per share of RMB6.31, in the same period of 2012.

Now I would like to highlight a few key items in the balance sheet, as at June 30, 2013.

Cash and bank balances were RMB3.98 billion, US$644.3 million, compared with RMB3.16 billion at December 31, 2012.

Short- and long-term borrowings were RMB2.56 billion, US$414.7 million, compared with RMB2.45 billion at the end of 2012.

Net inventory was RMB1.98 billion, US$320.8 million, compared with RMB2.01 billion at the end of 2012.

With that, Operator, we are ready to begin the Q&A session.

QUESTIONS AND ANSWERS

Operator

Thank you. We will now begin the question and answer session. (Operator Instructions).

Our first question comes from the line of Alex Potter, Piper Jaffray. Please go ahead.

Alex Potter - *Piper Jaffray - Analyst*

Hi, guys. I was wondering if you could chat first of all on the National IV emission standard. There's been now, I guess, a little over one month since the standard went into effect. Have you seen an impact on sales of National IV-compliant engines; has there been an uptick in the last month?

Weng Ming Hoh - *China Yuchai International Limited - President*

Okay. Hi, this is Weng Ming here. Okay, as you know the National IV standards have been implemented in China, but implementation is a little bit patchy. So far we see a lot of pre-buying for National III engines, I haven't seen National IV being sold in a big way yet.

Alex Potter - *Piper Jaffray - Analyst*

Okay. So does that basically mean that if there hasn't been any new sales of National IV engines in the months since the standard was implemented, does that mean that the standard basically isn't being enforced at all, if you are not selling any?

Weng Ming Hoh - *China Yuchai International Limited - President*

Well, you can't say that, right. I'm sure the Government is doing something about it. But I think because of the pre-buying in June, I'm sure that will have an impact on the sale of National IV going into the second half.

Alex Potter - *Piper Jaffray - Analyst*

Okay. All right, so I guess then another way to look at this is you expect -- because clearly if you are not selling any National IV engines and you are no longer selling any National III engines, after the standard, then your volume must be going down very, very substantially right now. Is that true?

Weng Ming Hoh - *China Yuchai International Limited - President*

We had a healthy July. The July sales have been pretty healthy, but the second half of the year we expect it to be quite challenging, because I think (inaudible) the Chinese economy is quite challenging for the second half.

Alex Potter - *Piper Jaffray - Analyst*

Right. Okay, so if there was a healthy July, what was it you were selling? If you weren't selling National IV engines, then you must have been selling National III engines that don't comply with the standard.

Weng Ming Hoh - *China Yuchai International Limited - President*

We are selling -- we also have other engines that we sell, things like the bus engines that we sell, with quite large quantity most months. We have off-road engines, the agriculture engines seem to be picking up this first six months also, now. But this National IV engines, we do sell some in smaller quantities, particularly there's demand in the big cities, like the Tier 1 cities.

Alex Potter - *Piper Jaffray - Analyst*

Okay. Okay, so you are getting National IV engine sales just -- only in the Tier 1 cities?

Weng Ming Hoh - *China Yuchai International Limited - President*

Yes, we do have some.

Alex Potter - *Piper Jaffray - Analyst*

Okay. Okay, and then I was wondering also, when it comes to meeting those National IV standards, whose SCR system are you using?

Weng Ming Hoh - *China Yuchai International Limited - President*

I'll let our VP Operations answer this.

Alex Potter - *Piper Jaffray - Analyst*

Okay.

Kelvin Lai - *China Yuchai International Limited - VP, Operations*

Well, hi, Alex. The SCR and that at the moment that we still are using are from the imports. And the -- we also and the buying some components and then we're building by ourselves as well. So that depends on the OEM's option.

Weng Ming Hoh - *China Yuchai International Limited - President*

Yes.

Alex Potter - *Piper Jaffray - Analyst*

Okay. Right. Okay, and then can you remind me again -- I know that -- I think I heard you say this, but I didn't hear quite clearly. How many natural gas engines did you sell in the quarter? I think I heard 13,000

Weng Ming Hoh - *China Yuchai International Limited - President*

That's correct.

Alex Potter - *Piper Jaffray - Analyst*

-- I didn't know if that was -- so that was in the quarter?

Weng Ming Hoh - *China Yuchai International Limited - President*

Yes, for the half year, not the quarter.

Alex Potter - *Piper Jaffray - Analyst*

Okay. And the other question --

Weng Ming Hoh - *China Yuchai International Limited - President*

(Multiple speakers), sorry.

Alex Potter - *Piper Jaffray - Analyst*

Okay, okay, that's -- okay. And do you think that now, with National IV going into effect, do you think people are going to be buying natural gas engines, instead of buying National IV diesel engines, as the way to meet the standard?

Weng Ming Hoh - *China Yuchai International Limited - President*

Well, I guess that there is a good chance of that happening, the reason being that the running cost of the natural gas engine is a lot cheaper than National IV. And the cost of the differential within National IV and that of our natural gas engines is smaller than between the National III and gas engine. So there is a good chance that the... it goes there.

Alex Potter - *Piper Jaffray - Analyst*

Okay. Can you give me rough numbers in terms of the percent, so if you've got a natural gas engine, how much does that cost in relation to a National III engine and a National IV engine, just in maybe percentage terms?

Kelvin Lai - *China Yuchai International Limited - VP, Operations*

Well, I think there's a -- not a guideline as to what the price variation will be, because -- and you will be -- varies between the different manufacturers. That said, from our experience and the natural gas engine and then comparing with Nat IV engines, and then will be in the range of 10% to 15% higher. But for the National III engines they are even more expensive, because of the difference of emission standards.

Alex Potter - *Piper Jaffray - Analyst*

Right, so that 10% to 15%, that was natural gas versus National III?

Kelvin Lai - *China Yuchai International Limited - VP, Operations*

IV.

Alex Potter - *Piper Jaffray - Analyst*

Okay, that's what I thought. Okay. All right -- let's see. I guess the last one I had was -- if you could give a contribution from heavy-duty engine units in the quarter, I know that you gave your full units sold at 141,000, or thereabouts. How much of that was heavy duty? Thanks.

Weng Ming Hoh - *China Yuchai International Limited - President*

Okay, I think it's about -- if we've got it -- I would say over [10%] (Company corrected after the conference call) of business is heavy duty.

Alex Potter - *Piper Jaffray - Analyst*

Over 30%?

Weng Ming Hoh - *China Yuchai International Limited - President*

10% (Company corrected after the conference call).

Alex Potter - *Piper Jaffray - Analyst*

Okay. Okay, thank you very much.

Operator

Thank you. And our next question comes from the line of David Raso of ISI Group. Please, go ahead.

David Raso - *ISI Group - Analyst*

Hi, hello. My two questions are -- one, how many months at the current selling rate in the industry -- how many months of National III engines do you think are already in the channel?

Weng Ming Hoh - *China Yuchai International Limited - President*

That's a difficult question, David. I find it hard to estimate that one.

David Raso - *ISI Group - Analyst*

Just at least get some flavor around it, do you feel half-year growth in the second quarter was pre-building to serve demand in the second half? We're just really trying to get a feel for how long will it take to work through the transition at your customers, if we assume a certain adoption rate of NS IV. Can you give us a little bit of color around it?

Weng Ming Hoh - *China Yuchai International Limited - President*

Well, yes, I guess it depends on how strictly the government enforce the National IV engine standards, David. So in the first-tier cities, it will be enforced very strictly. However, when you go to Tier 3 and 4 cities, it's hard to say. Just I think a lot of it depends on the local government. So it's hard to even gauge as to how many months is in the inventory; I would hesitate to estimate.

David Raso - *ISI Group - Analyst*

Maybe ask another way. If I think of the industry geographically, across the country, whatever you want to consider to be normal selling rates in each region. The areas that have now adopted NS IV, would be what percent of the Chinese truck market is now NS IV?

Weng Ming Hoh - *China Yuchai International Limited - President*

The NS IV is -- I would say the bulk of the users for NS IV are in the urban area in the big Tier 1 cities.

David Raso - *ISI Group - Analyst*

(Multiple speakers) about 30%, you say?

Weng Ming Hoh - *China Yuchai International Limited - President*

(Multiple speakers) long-range, long-range travel that would be. Again, it is difficult to estimate, David. I would hesitate to estimate.

David Raso - *ISI Group - Analyst*

Just to get a rough idea, because I'm not sure which cities are in really enforcing it in a strong fashion.

Weng Ming Hoh - *China Yuchai International Limited - President*

Those Tier 1 cities, like Beijing, Shanghai, Guangzhou, those are the big cities so definitely enforcing it -- (multiple speakers).

Kelvin Lai - *China Yuchai International Limited - VP, Operations*

Let me -- try to explain this way -- David, this is Kelvin.

David Raso - *ISI Group - Analyst*

Hi.

Kelvin Lai - *China Yuchai International Limited - VP, Operations*

I think that in Beijing they are already in the National IV, so they are ahead of the other cities. But in Guangzhou and they just announced that they will be -- have a grace period of three months of time.

So I think this will depend on the city from city. It's difficult to put a guideline at this stage, because during the announcement of the implementation of Nat IV and then the government decision to put a day on the banning of the registration of the Nat III engine. So that's -- and then you give a lot of room to the local government and then to play with. So at this stage really and then we don't know which city will implement tomorrow or not.

David Raso - *ISI Group - Analyst*

Could you -- I know it's hard to predict what the government is going to do, so I know it's not a fair question. But January 1 of 2014, for your business planning, what percent of the market do you expect to be NS IV January 1?

Kelvin Lai - *China Yuchai International Limited - VP, Operations*

Again, and we cannot forecast on that way, David. But I can -- what we can say now is we actually -- we had a discussion with all the OEMs and then we had all our engines have been -- worked with the -- those vehicles and then using the Nat IV as a public announcement, the "GongGao" in the system.

So we are ready here, and the -- but at this stage -- and then we -- what I can say is our engine delivery is still on basis of the OEM orders, instead of the doing the stocks for the Nat IV because we don't really see that the real implementation date.

David Raso - *ISI Group - Analyst*

I know these are hard questions, because the government has left you in a difficult situation, so I apologize. But the order book that you have right now, what percent is NS IV, and when are your OEM customers at least trying to give you some insight on when it might shift more towards NS IV?

So again, the current order book for heavy; how much is NS IV, as percentage?

Weng Ming Hoh - *China Yuchai International Limited - President*

Well, we don't see a very high order book yet for National IV right now -- as of today. Then again, we don't have orders that goes into next year. So it's not high at the moment.

David Raso - *ISI Group - Analyst*

The last question, to think about the revenue sequentially in the second half, I would think the third quarter you still have some inventory of NS III that you can continue to sell, in markets that aren't really enforcing NS IV, and are still ordering NS III. And you can still make all the NS III you want for the geographies that haven't enforced NS IV, correct?

Weng Ming Hoh - *China Yuchai International Limited - President*

Yes.

David Raso - *ISI Group - Analyst*

So the sequential revenue, as long as the market is not really enforcing NS IV, thus they are not ordering NS IV, the sequential decline should really only be a function of just what end demand is naturally, and how much pre-buying was taking place. So I'm just trying to get a better feel for the sequential inventory decline, in a way, by who's enforcing it. It doesn't sound like a lot of cities are enforcing it that hard. And how much of your second quarter growth was as a pull forward, so maybe at a minimum how much of the second quarter do you think was a pull forward, just to help a bit with the modeling for the rest of the year?

Weng Ming Hoh - *China Yuchai International Limited - President*

Well -- it's again -- I'm not trying to evade your question, David, but we're really finding it a bit difficult at this point to really judge the market. Simply because when you have only had one month of it, and there was quite a lot of pre-buying before that, and how the government is going to enforce this National IV engine is not very clear right now, okay?

From what we understand they are leaving some of this enforcement to the local government, depending on how ready those localities are. So there is quite a fair bit of uncertainties in this.

David Raso - *ISI Group - Analyst*

Yes, I'm sorry to labor the point, but it's difficult for you to set your production schedule the same way it's difficult for us to figure out the real end demand for the second half.

Weng Ming Hoh - *China Yuchai International Limited - President*

Yes.

David Raso - *ISI Group - Analyst*

As long as the government is not yet enforcing the NS IV, but there's a concern by customers that it's coming, wouldn't there continue to be some pre-buying then in the third quarter, and really up until the moment the government does truly enforce it? Like are orders already lower, sequentially?

Weng Ming Hoh - *China Yuchai International Limited - President*

The question -- I would think that the National IV engines will go up a little bit more than before, will sell more than before simply because the big cities, like Shanghai and Beijing, even Tianjin and now Guangzhou, they will be enforcing National IV, okay? So that will force up the sales of National IV somewhat, over the next two to three months. But by how much, and how it is going to affect the industry, it's really hard to gauge.

David Raso - *ISI Group - Analyst*

But for base case, we should assume some sequential decline? Is that a fair assessment?

Weng Ming Hoh - *China Yuchai International Limited - President*

Yes, yes, that's fair. It's fair to assume some sequential decline in (multiple speakers), yes.

David Raso - *ISI Group - Analyst*

I appreciate the time. I know it's a little tricky right now for the next couple of quarters. So thank you very much, I appreciate it.

Weng Ming Hoh - *China Yuchai International Limited - President*

Yes, thanks, David.

Operator

Thank you. And our next question comes from the line of Emmett Wright from Milwaukee Private Principal. Please go ahead.

Emmett Wright - *Milwaukee Private Wealth Management - Analyst*

And I do need to labor the point on the National IV. With respect to what the government chooses to do or not do, what are the expectations of your management team in terms of the enforcement of National IV? And what does your business plan call for with respect to production and output for National III versus IV engines?

Kok Ho Leong - *China Yuchai International Limited - CFO*

We are expecting to see -- see some demand for National IV to increase as the enforcement -- as we go into the remainder of the year, even to next year, simply because as more and more local government enforce the National IV standard, I think the demand will go up. Now the timing, the timetable, we haven't seen any yet.

Emmett Wright - *Milwaukee Private Wealth Management - Analyst*

How are your competitors reacting to this environment?

Kok Ho Leong - *China Yuchai International Limited - CFO*

Well, it's hard for us to comment what the competitors is going to do; we have no visibility as to how we can compare to do it. It would not be fair for us to comment.

Operator

All right, thank you. And our next question comes from the line of Mohit Khanna, from Value Investment Principals. Please go ahead.

Mohit Khanna - *Value Investment Principals - Analyst*

Good morning, guys. I had a question on the trade receivables -- what is an average age of the trade receivables we have on the book?

Kok Ho Leong - *China Yuchai International Limited - CFO*

Yes -- this is Leong here. Actually our account receivables has always been very healthy for those people who follow us. You can see that our account receivables are mainly with the larger OEM buyers, OEM makers they are all very established and big companies with cash in their bank, like the Dongfeng Group.

As for our aging, they are healthy. All of the aging are healthy and either they are in the healthy open accounts or they are giving us bank bills -- bills receivable that are backed by a bank.

So as far as I am concerned, I have not seen a change in the profile of our account receivables, except (multiple speakers) --

Mohit Khanna - *Value Investment Principals - Analyst*

So, so --

Kok Ho Leong - *China Yuchai International Limited - CFO*

-- bigger customers we may give them longer credit period, but that's backed by either their creditworthiness or bills receivable that are backed by the bank.

Mohit Khanna - *Value Investment Principals - Analyst*

So you think 95% to almost 100% are good?

Kok Ho Leong - *China Yuchai International Limited - CFO*

I would -- don't want to put the number to the final 100%, but it is significant portion of our accounts receivable belong to such a healthy category.

Weng Ming Hoh - *China Yuchai International Limited - President*

Okay, we have a question here from our live audience. They are asking please give an indication of the total July engine shipments.

So all I can say at this point is that we had a healthy July shipment. It's better than the one we had last year same month, yes. Okay?

Operator

All right, thank you. We have now reached the end of our Q&A session and I will turn the call back over to Mr. Hoh.

Weng Ming Hoh - *China Yuchai International Limited - President*

Okay, thank you all for participating in our second quarter and half year ended June 30, 2013 conference call. We look forward to speaking with you again. Goodbye.

Operator

Thank you. Ladies and gentlemen, that does conclude our conference for today. Thank you for participating. You may all disconnect.
