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PAKISTAN
AUTOS

REP-019
MARKET
VISTA

PSMC: Demand upcycle couldn't come sooner

- **Recent sales numbers reflect the resilient nature of domestic vehicle sales where, while the same cannot be said for PSMC's numbers (10MCY20 cumulative sales volume dip of 53%YoY vs. 48% for PC sales), we find some saving grace in Oct'20 sales stabilizing their downslide (-13%YoY vs. CYTD avg. of -48%YoY with Alto sales up ~5%YoY).**
- **Additionally, macro stability coupled with low interest rates are driving the start of another upcycle in vehicle sales, where we believe PSMC is likely to be a beneficiary, but may face significant hurdles from new entrants amid price sensitive consumers holding off on making major purchase decisions**
- **In this backdrop we revise our sales estimates across the forecast horizon (unit sales CAGR over CY20-25 of 10.1% vs. 5.5% previously) while significantly shortening the path back to profitability (CY20/21 earnings raised by 30/65%) raising our DCF based TP to PkR180/sh.**
- **We have built in the weak earnings outlook, reflected in tepid unit sales assumptions (~76K unit sales for CY21) with the slowdown in LCV sales expected to persist (Bolan/Ravi demand expected to rise 40%YoY but stay below 9K units respectively), where major policy incentives are hard to forecast (bulk orders could lend upside risks).**

Performance Review: 9MCY20 results remain in the red (cumulative LPS of PkR31.58/sh), where key highlights were: 1) major bounce back in 3QCY20 GMs (5.2%, best Q since 4QCY18) pulled cumulative GM's into positive territory (2.2% GM vs. 2.2%/1.7% during 9MCY19/CY19) where sustainability remains questionable, particularly due to a period of PkR volatility, 2) ~44% YoY fall in revenues as unit sales slipped (56.2%YoY) while the average sales price tag rise of 26.6% failed to fortify margins and, 3) spike in finance cost of 2.3xYoY for 9MCY20 were emblematic of reliance on short term borrowing to fulfill working capital drains.

Swift facelift is a non-event: Swift remains a relatively stable contributor to the OEMs sales since its launch in CY10 (CY15-19 average revenue weight of 3.5%), while maintaining a similar share on a unit sales basis (CY14-18 average of 3.5%), making the variant a profit center for the OEM (largely from consistent price hikes over the period). In terms of a face-lift the much awaited launch of an upgraded variant is likely to benefit from the new-model effect, where a hike in the price tag and unit sales growth is accretive for profitability. That said, the segment remains tough terrain for PSMC where the brand has struggled to compete with well-entrenched HCAR and INDU, with both competitors having launched or are in the process of launching new variants in the space. While details of the planned launch remain sparse and management is not expected to confirm this development (following industry norms) we await dealer level confirmation before crystalizing the launch in our estimates.

Segment concentration of its own making: Considering the OEM has concentrated its variants at the lower end of the price and displacement spectrum for CKDs, we highlight the troubled path PSMC faces in regaining market share. To recall, demand dynamics of the segment have always been dominated by price conscious buyers, with the tilt to Suzuki variants primarily led by: 1) strong dealer network, 2) after sales support and low maintenance cost, including the cost of parts, and 3) comparably lower lead times for delivery for on-the-run variants. On all these counts deep-pocketed new entrants (KIA in particular) have dented PSMC's standing.

Investment Perspective: In this backdrop we revise our sales estimates for across our forecast horizon (unit sales CAGR over CY20-25 of 10.1% vs. 5.5% previously) while significantly shortening the path back to profitability (CY20/21 earnings raised by 30/65%) raising our DCF based TP to PkR180/sh, implying a Sell stance to last close. The stock has corrected 16%CYTD in part by a weak outlook, reflected in tepid unit sales assumptions (~76K unit sales for CY21, ~51% utilization despite new Swift launch) with the slowdown in LCV sales expected to persist (Bolan/Ravi demand expected to rise 40%YoY but stay below 9K units respectively), where major policy incentives or hard to forecast bulk orders could lend upside risks.

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SELL

TARGET PRICE (PkR)	SHARE PRICE (PkR)
180.00	190.84
UPSIDE/DOWNSIDE	**DIV. YIELD**
-5.6%	-

PSMC: Valuation snapshot

	CY19A	CY20F	CY21F	CY22F
EPS New	(35.45)	(27.15)	(2.71)	4.94
EPS Old		(38.81)	(7.73)	3.75
%Change		30.0%	64.9%	31.7%
GM	1.7%	1.9%	5.4%	6.6%
NM	-2.5%	-3.2%	-0.3%	0.4%
Sales Growth	-2.8%	-41.0%	14.0%	16.4%
ROE	-11.2%	-9.4%	-1.0%	1.7%
CKD Unit Sales Assumptions	109,858	57,951	75,633	87,297
BVPS	315	288	285	290

Source: Company Report & AKD Research

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- Discounted Cash Flow (DCF, DDM)
- Relative Valuation (P/E, P/B, P/S etc.)
- Equity & Asset return based methodologies (EVA, Residual Income etc.)

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