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PAKISTAN
Autos

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MARKET
VISTA

Non-filer ban is 'sink-or-swim' for OEMs

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- **Citing sizeable headwinds from cost pressures resulting in price hikes, accompanied by rising inflationary pressures hitting buying power and the recent ban on sale of new cars to tax non-filers, we revise down our estimates for automotive sales.**
- **Revising our sales growth assumption for CY18/FY19 onwards, we bring down earnings by ~14.5%/~10.2% across our forecast horizon, resulting in FCFE based TPs being cut by 25%/11% to PkR347/1,866/sh for PSMC/INDU, where the relative resilience of premium passenger car OEMs (1,300CC and above segment) is at play.**
- **Limits to pricing power hampering earnings growth, flows through to lower GM assumptions, as competitive 'moats', i.e. after sales services and vehicle availability gain prominence.**
- **Even so, as both PSMC and INDU have plunged 37% and 18% CYTD, we believe current price levels have largely accommodated dampeners to demand (PSMC/INDU trade at forward P/Es of 8.2/6.6x), with our revised TP' offering capital upside of 11/38% accompanied by D/Ys of 3.2/9.5%, making for Neutral/Buy calls, respectively.**
- **We flag developments on new vehicle launches, CAPEX plans, LCV sales and margin preservation as major indicators to monitor over the near term.**

PSMC & INDU estimate revisions

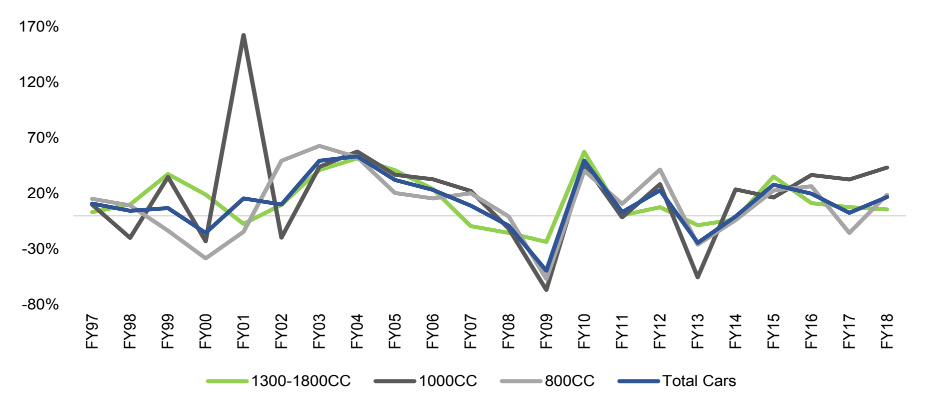
	EPS(PkR)				
PSMC	CY17A	CY18F	CY19F	CY20F	TP(PkR)
Old	46.5	40.8	43.1	32.2	465.5
New	-	38.1	32.2	30.5	346.6
Change	-	-6.6%	-25.3%	-5.4%	-25.5%

	EPS(PkR)				
INDU	FY18A	FY19F	FY20F	FY21F	TP(PkR)
Old	200.7	215.0	226.0	238.2	2,085.0
New	-	204.6	204.6	199.4	1,866.0
Change	-	-4.8%	-9.5%	-16.3%	-10.5%

Source: Company Reports & AKD Research

Confirmed non-filer sales ban makes a bad situation worse: Auto sales are headed towards a down cycle (8MCY18 passenger car sales average +1%MoM vs. +5%MoM for 8MCY17), brought on by: i) price hikes of 7-12%CYTD for all OEMs on account of PkR depreciation and levies on auto part imports, ii) absence of any new model launches, where the last major launch was the revamped Cultus in April'17, and iii) the general decline of purchasing power as monetary tightening makes auto financing less attractive. Adding to industry woes, the ban on sale of new vehicles to non-filers with the revenue authority was 'the straw that broke the camel's back' as we asserted after the August'18 sales decline in the PC segment (falling 19%MoM/18%YoY).

800CC and below segment is most sensitive to cycles



Source: PAMA & AKD Research

Premium players better off: Bifurcating passenger car demand for the last 23yrs by segment, we highlight the relatively softer cycles for sales growth exhibited by the 1,300CC and above segment. Between FY96-18 four clear cycles can be seen for passenger car sales growth, they are 1) FY96-00, 2) FY01-09, 3) FY10-13 and 4) FY14 onwards, with the average cycle lasting 5yrs. Taking cues from these trends, we believe players in the premium segment will be relatively better off when facing the current bout of dampeners to demand.

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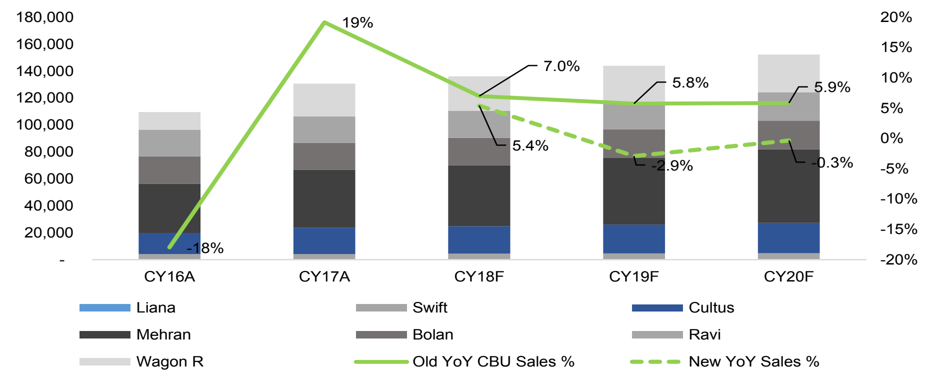
1,300CC segment is relatively resilient in down cycles

Cycles	Years	Total Passenger Car Sales			1300cc +			800CC-1000CC		
		Cycle average	Upcycle average	Downcycle Average	Cycle average	Upcycle average	Downcycle Average	Cycle average	Upcycle average	Downcycle Average
FY97-00	4	2%	7%	-16%	12%	17%	-7%	-7%	12%	-26%
FY01-09	9	15%	28%	-29%	15%	34%	-16%	17%	37%	-29%
FY10-14	5	10%	25%	-13%	11%	22%	-6%	13%	31%	-15%
FY15-18	4	17%	17%	NA	15%	15%	NA	13%	23%	-15%
Average		**11%**	**19%**	**-19%**	**13%**	**22%**	**-10%**	**9%**	**26%**	**-21%**

Source: PAMA & AKD Research

TPs for INDU/PSMC cut 25/11%: Revising our sales growth assumption for CY18/FY19 onwards, we bring down earnings for PSMC/INDU by ~14.5%/~10.2% across our forecast horizon, resulting in FCFE based TPs being cut by 25%/11% to PkR347/1,866/sh. Additionally worrisome developments regarding pricing power hinder earnings growth, prompting a cut in our GM assumptions to long term average levels of 7.2%/16.3% for PSMC/INDU, as competitive 'moats', i.e. dealer networks, after sales services, add-on features and vehicle availability become mandatory for sustaining market shares.

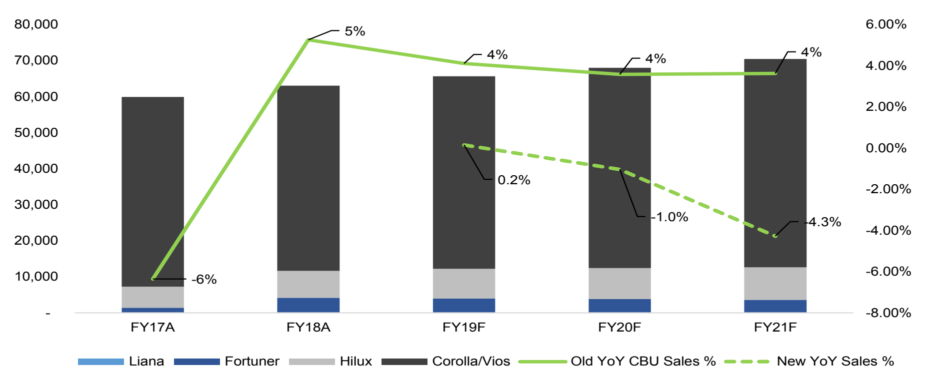
PSMC: Sales fall ~6% … LCV/Pickup segment have the potential to hold



Source: PAMA & AKD Research

Outlook: Numerous stakeholders stand to play their part in implementing the ban, while the amended Finance Bill goes on to impose punitive measures on companies violating the sales ban. Additionally, on the question of new entrants, it follows that they are likely to feel the heat of reduced demand as well. Developments we flag for close observations that need to be monitored in the near term: i) unintended consequences on pulling LCV sales lower, ii) responsiveness of OEMs to cost pressures, iii) new vehicle/model launches by existing OEMs (Vios and new Alto for INDU and PSMC), and vi) ability of assemblers to preserve margins as the long term competitive environment heats up (new entrants with large CKD assembly capacities to enter the market by CY20).

INDU: Steep taper for SUVs sales ...total sales decline of ~4% in FY21F



Source: PAMA & AKD Research

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