

Autos Sep'21 quarterly earnings preview

Automobile Assembler

Under Review

October 25, 2021

Key Points

- We present earnings expectations for our Auto sector universe (INDU, HCAR and PSMC) for the quarter ended Sep'21 where the combined earnings of the sector are expected to register 2.9xYoY/19%QoQ growth.
- The expected growth in earnings is mainly attributable to overall higher sales, which surged by 67%YoY/41%QoQ mainly led by PSMC (Sales tax reduction in budget FY22) followed by INDU (strong brand image) and HCAR (commencement of new City bookings).
- Gross margins of our coverage companies are estimated to remain relatively flat at 8% as against the previous quarter and increase 1% on yearly basis despite the sharp rise in volumes. We opine this flattish gross margin is mainly attributable to 6.40%QoQ PKR devaluation and sky rocketing commodity prices.
- Given steep devaluation of PKR/USD, rising raw material prices, higher freight charges, government intervention to avoid further price hike and global shortage of semiconductors, we foresee demand to slow down in the near future however, recent reduction of FED, sales tax, and lower auto prices, improving purchasing power parity and healthy farmer yields could provide some relief.

Next OEMs earnings to increase by 2.90xYoY to PKR6.86bn

Leading automobile assemblers including INDU, PSMC and HCAR are all slated to announce their financial result for the quarter ending Sep'21, soon. Overall, we anticipate that net earnings of Next Auto Universe (INDU, HCAR, PSMC) are likely to register a strong rebound during the quarter under review both on YoY and QoQ basis. The combined profit after tax (PAT) is estimated to witness a 2.90x increase to PKR6.86bn compared to PKR2.36bn of Sep'20 and PKR5.75bn of Jun'21. The rise in earnings is mainly attributable to recovery in unit sales backed by higher demand amid incentives announced in FY22 budget and normal business operations (compared to lockdown in SPLY), new model launches, high auto financing and favourable economic condition.

Sales remained upbeat

Unit sales during the quarter under review have witnessed a significant increase, both sequentially and on a yearly basis. Combined sales of our universe improved to 66,249 units as compared to 36,635/44,178 units during Sep'20/Jun'21, an increase of 81%YoY/50%QoQ. Individually PSMC, INDU and HCAR witnessed a strong recovery in sales where they posted increase of 2.2xYoY, 59%YoY and 23%YoY, respectively. In addition, both PSMC and INDU recorded the highest ever quarterly unit sales, surpassing the peak volumes seen back in 2018. Thus, we foresee, industry revenue to clock in at PKR137bn, as compared to PKR77bn in the corresponding period last year and PKR99.7bn in preceding quarter. Having said this, gross margins are likely to remain flat on sequential basis despite sharp recovery in unit sales due to rising steel prices, PKR depreciation, and higher freight charges.

Inflationary pressures outweigh increase in volumes

We expect gross profit in absolute terms to increase to PKR10.9bn compared to PKR4.8bn of Sep'20 and PKR9.2bn of Jun'21. Moreover, gross margins of our coverage companies are estimated to remain relatively flat at 8% as against the previous quarter and increase 1% on yearly basis despite the sharp rise in volumes. We opine, this flattish gross margin is mainly attributable to 6.40%QoQ PKR devaluation and sky rocketing commodity prices. Since Automobile sector is largely dependent on parts and raw materials from abroad where Japan and Thailand are the two major hubs, the global chip shortage and unfavourable weather conditions may lead to supply chain disruptions in the coming quarter as well, which could negatively impact plant operations. Furthermore, inability to pass on the complete cost inflation due to government interventions and demand sensitivity, may further exacerbate the situation.

Outlook

Given steep devaluation of PKR/USD, rising raw material prices, higher freight charges, government interventions to avoid further price hike and global shortage of semiconductors chips, and uptick in interest rates, we do not rule out demand to slow down in the near future with continued longer delivery times, however, recent reduction in prices after the reduction in tax and duties, improving purchasing power parity and healthy farmer incomes will provide some relief. On economic front, an increase in monetary tightening coupled with revision in prudential regulation of consumer financing may pose risks to industry volumes we

Pakistan Equities Automobile Assembler

Key Data

Mkt. Cap. (USDmn)	1,730
Mkt. Cap. (PKRbn)	301
Index Weightage (KSE-100)	3.0%
Number of Listed Companies	12

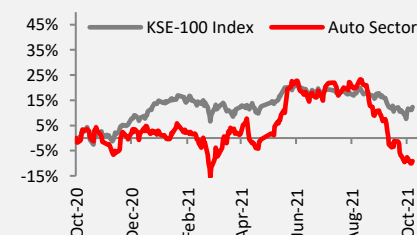
Source: PSX, Next Research

Sep'21 Sector Estimates

EPS	Sep'21	YoY	QoQ	DPS
INDU	62.69	2.67x	12%	40
HCAR	8.43	83%	30%	-
PSMC	8.96	n/a	76%	-

Source: Company Accounts, Next Research

1 Year Relative Performance




Source: PSX, Next Research

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think, out of total car sales in Pakistan, around 49% of the sales are of over 1,000cc, so in this context HCAR is likely to be hit most by these measures as auto financing contributes around 45-50% of their total sales. Moreover, with the influx of foreign entrants, new launches are expected to hit in the latter half of the year with KIA being more active and planning to introduce another vehicle by the fiscal year end. In addition, most of the ongoing launches are in SUV category and with prices that are almost at par with the existing players offering in the sedan segment. We think, pricing power of incumbent players will get tested and especially the ones having price sensitive in the market may have to be more cautious in their approach. Hence, shift in consumer preference cannot be ruled out in this regard.



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Over Weight	> Weight in KSE 100 index
Market Weight	= Weight in KSE 100 Index
Under Weight	< Weight in KSE 100 Index

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Where;

$R = \text{Expected Dividend Yield} + \text{Expected Capital Gain}$

R' is before tax

Investment horizon is between six months to twelve months

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