

21 May 2018 | 1Q18 Result Review

Tan Chong Motor

Turnaround potential grossly underestimated

- **1Q18 beats consensus**
- **Returns to profits after 2-year losses, underpins BUY thesis**
- **Best proxy to stronger RM, consensus grossly underestimating Tan Chong's earnings turnaround potential**
- **New launches nicely timed for expected improved sentiment**
- **Contrarian BUY re-affirmed at unchanged TP of RM2.05**

Beats consensus. Tan Chong 1Q18 was in-line with ours but beat consensus estimates. The group reported net profit of RM4m for its 1Q18 accounting for 21% of our FY18F and ahead of consensus' loss forecast.

Turns to the black. After 2 consecutive years of losses, Tan Chong returned to the black in 1Q18, underpinning our BUY thesis on the stock. These are sustainable profits given: (1) Inventories of old Almera (bought at expensive forex) would have largely been run down (2) Sustained Ringgit strength (3) Discounting has been rolled back given normalising inventory levels now. EBITDA margins improved further to 5.2% from 1.6%/4.8% 1Q17/4Q17.

Operating cash almost doubled. Inventory levels reduced further to RM1.1b, and coupled with improved profitability, operating cash flow grew some 75%yoy to RM140m. This positions Tan Chong well to re-invest in growth going forward, particularly for new model lines and stock build-up given a resumption of new launches this year.

New launch kickstarted with the SHybrid. New launches (after a 2-year lull) were kickstarted by the new Serena S-Hybrid last Monday. The S-Hybrid is a CKD and EEV-certified – meaning Tan Chong will benefit from EEV duty rebates, which will drive margin improvement. Based on news reports, other new models slated for launch are the new Nissan Leaf and more importantly, a B-segment SUV/crossover model. Tan Chong's new launches are nicely timed ahead of an expected improvement in consumer sentiment from the abolishment of GST.

Indochina losses narrowed. Vietnam, which accounts for the majority of Indochina operations, saw losses narrow 40%yoy on the back of a 16%yoy rise in revenue.

Consensus underestimating Tan Chong's turnaround. Earnings should strengthen further in the next few quarters given stronger Ringgit levels (now ~RM3.90 vs. 1Q18E: RM4.16). The next leg up for earnings will come from new model launches in the coming quarters after a 2-year lull. We forecast Tan Chong to return to profits in FY18F and to register more meaningful earnings in FY19F. Our forecasts have yet to factor in the new model launches this year. For now, we forecast a conservative 1.8%/2.1% Nissan TIV growth over FY18F/19F. Our FY19F is 27% above consensus, while for FY18F, consensus is still expecting a loss vs. our profit forecast of RM21m.

Maintain BUY

Unchanged Target Price: RM2.05

RETURN STATS

Price (18 May 2018)	RM1.67
Target Price	RM2.05
Expected Share Price Return	+22.8%
Expected Dividend Yield	+1.8%
Expected Total Return	+24.6%

STOCK INFO

KLCI	1,854.50
Bursa / Bloomberg	4405 / TCM MK
Board / Sector	Main/Automotive
Syariah Compliant	Yes
Issued shares (mil)	652.66
Market cap. (RM'm)	1,089.94
Price over NA	0.40
52-wk price Range	RM1.29-1.87
Beta (against KLCI)	0.85x
3-mth Avg Daily Vol	0.03m
3-mth Avg Daily Value	RM0.06m
Major Shareholders (%)	
Tan Chong Consolidated	40.4
EPF	6.0
Nissan Motor	5.7

MIDF RESEARCH is a unit of MIDF AMANAH INVESTMENT BANK

Kindly refer to the last page of this publication for important disclosures

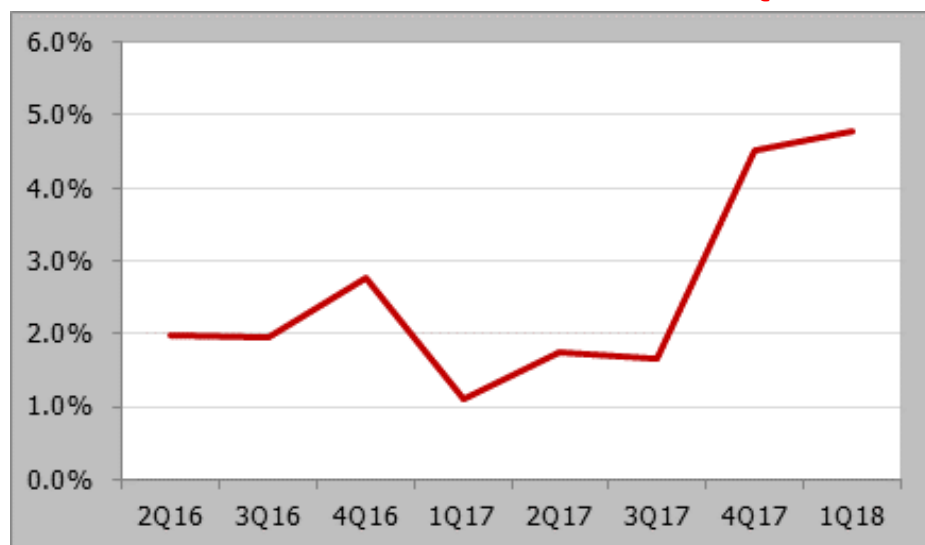
INVESTMENT STATISTICS

FYE Dec	FY15	FY16	FY17	FY18F	FY19F
Revenue (RM'm)	5,716.7	5,510.7	4,341.2	4,809.1	4,916.3
EBIT (RM'm)	169.0	18.7	(18.7)	70.0	124.4
Pre-tax Profit (RM'm)	115.3	(43.1)	(72.8)	27.2	81.2
Core net profit (RM'm)	59.9	(58.8)	(88.6)	20.5	60.5
FD EPS (sen)	8.9	(8.8)	(13.2)	3.1	9.0
EPS growth (%)	(20.9)	NA	NA	NA	194.7
PER (x)	18.7	(19.1)	(12.7)	54.7	18.5
Net Dividend (sen)	5.0	2.0	2.0	3.0	3.0
Net Dividend Yield (%)	3.0	1.2	1.2	1.8	1.8

Source: Company, MIDF

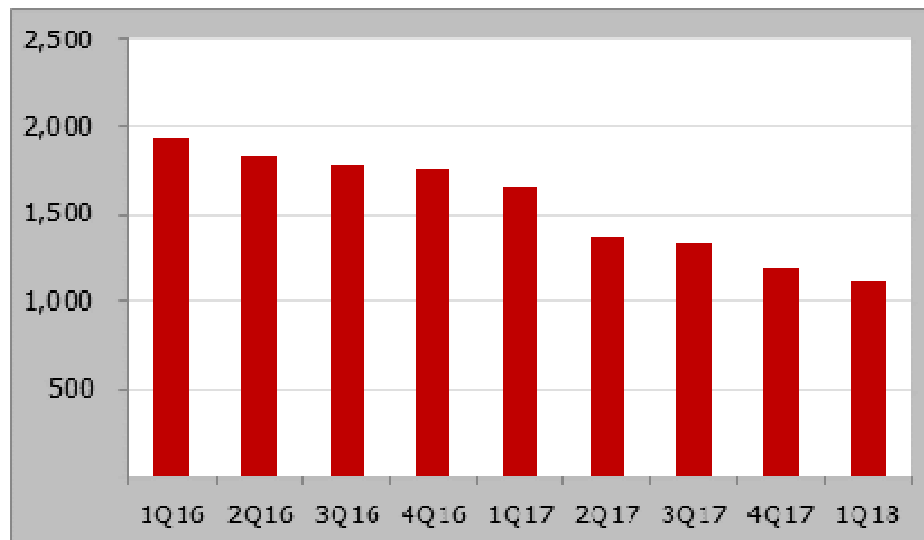
Recommendation. Re-affirm our contrarian BUY at unchanged TP of RM2.05 conservatively pegging Tan Chong to trough PBV of 0.5x. Having seen share price fall some 40% in the past 24 months, Tan Chong now trades at just 0.4x FY18F PBV (which is lower than even its historical trough PBV of 0.5x) amid a turnaround in earnings from FY18F onwards. Key catalysts: (1) Resumption of new model launch from FY18F (2) Sustained Ringgit strength (3) Further narrowing in losses from Indochina operations (4) A bottoming in market share.

EXHIBIT 1: EBITDA MARGIN IMPROVED FURTHER IN 1Q18



Source: Company, MIDF

EXHIBIT 2: INVENTORIES SUCCESSFULLY REDUCED IN PAST 2 YEARS (RM MIL)



Source: Company, MIDF

EXHIBIT 3: TAN CHONG 1Q18 RESULT SUMMARY

YE Dec (RMmil)	1Q17	4Q17	1Q18	QoQ %	YoY %
Revenue	995.7	1,076.0	1,034.6	-3.8%	3.9%
Operating profit	(22.2)	27.1	23.6	-12.7%	NA
Interest expense	(16.7)	(18.2)	(16.1)		
Interest income	2.9	2.6	4.2		
Associates	0.4	1.1	1.7	53.8%	317.8%
Pretax profit	(35.5)	12.6	13.5	6.9%	NA
Tax expense	(1.9)	(18.8)	(11.4)	-39.6%	493.3%
Minorities	(2.1)	1.0	(2.2)	-326.2%	1.3%
Net profit	(35.3)	(7.2)	4.3	-159.1%	NA
Core net profit	(35.3)	(7.2)	4.3	NA	NA
EPS (sen)	(5.3)	(1.1)	0.6		
Gross DPS (sen)	0.00	1.00	0.00		
Operating margin (%)	-2.2%	2.5%	2.3%		
Core operating margin (%)	-0.7%	3.9%	3.7%		
Pretax profit margin (%)	-3.6%	1.2%	1.3%		
Net profit margin (%)	-3.5%	-0.7%	0.4%		
Tax rate (%)	5.4%	-149.5%	-84.5%		
Nissan TIV (units)	5,989	6,395	5,310	-17.0%	-11.3%
RM:USD (Spot, delayed by 3-month)	4.45	4.26	4.16	-2.3%	-6.5%
Revenue/vehicle (RM000)	163.1	165.1	189.7	14.9%	16.3%
Operating profit/vehicle (RM000)	-3.7	4.2	4.5	NA	-220.1%
Net profit/vehicle (RM000)	-5.9	-1.1	0.8	NA	-113.6%
Operating cost/vehicle (RM000)	170.0	164.0	190.4	16.1%	12.0%

Source: Company, MIDF

EXHIBIT 4: TAN CHONG 1Q18 RESULT SUMMARY (BREAKDOWNS)

YE Dec (RMmil)	1Q17	4Q17	1Q18	QoQ %	YoY %
Autos	976.6	1,055.7	1,007.1	-5%	3%
Financial Services	16.8	18.6	24.8	33%	47%
Others	2.3	1.6	2.7	70%	21%
Total revenue	995.7	1,076.0	1,034.6	-4%	4%
Autos	10.6	47.8	48.2	1%	353%
Financial Services	6.5	5.5	7.9	42%	21%
Others	(1.1)	(1.5)	(2.1)	40%	92%
Total EBITDA	16.0	51.9	54.0	4%	237%
EBITDA margins	1.6%	4.8%	5.2%		
Autos	1.1%	4.5%	4.8%		
Financial Services	38.6%	29.7%	31.8%		
Others	-48.5%	-93.2%	-76.9%		
COUNTRY BREAKDOWN					
Malaysia	826.2		834.4	NA	1%
Vietnam	130.9		152.1	NA	16%
Others	38.5		48.1	NA	25%
Total revenue	995.7	-	1,034.6	NA	4%
Malaysia	24.5		54.6	NA	123%
Vietnam	(6.9)		(4.2)	NA	-40%
Others	(1.6)		3.5	NA	-327%
Total EBITDA	16.0	-	54.0	NA	237%
EBITDA margins	1.6%		5.2%		
Malaysia	3.0%		6.5%		
Vietnam	-5.3%		-2.7%		
Others	-4.0%		7.4%		

Source: Company, MIDF

Income Statement	FY15	FY16	FY17	FY18F	FY19F
Revenue	5,716.7	5,510.7	4,341.2	4,809.1	4,916.3
Operating expenses	(5,547.6)	(5,492.0)	(4,359.9)	(4,739.1)	(4,792.0)
EBIT	169.0	18.7	(18.7)	70.0	124.4
Net interest expense	(56.1)	(65.0)	(57.5)	(44.2)	(44.6)
Associates	2.4	3.2	3.4	1.5	1.5
PBT	115.3	(43.1)	(72.8)	27.2	81.2
Taxation	(45.4)	(16.0)	(23.6)	(6.4)	(19.9)
Minority Interest	(5.0)	4.1	(7.8)	(0.3)	(0.8)
Net profit	74.9	(54.9)	(88.6)	20.5	60.5
Core net profit	59.9	(58.8)	(88.6)	20.5	60.5
Consensus net profit	74.9	(49.0)	(93.7)	(1.6)	47.6
Balance Sheet	FY15	FY16	FY17	FY18F	FY19F
Non-current assets	2,406.6	2,684.7	2,933.9	2,548.4	2,558.1
PPE	1,704.2	1,863.0	1,832.6	1,841.5	1,849.7
Investments in associate	37.8	42.9	40.8	42.3	43.8
Others	664.7	778.8	1,060.5	664.7	664.7
Current assets	2,762.3	2,881.8	2,466.3	2,711.6	2,926.7
Inventories	1,645.2	1,762.8	1,186.0	1,058.0	1,229.1
Receivables	818.8	774.8	696.1	721.4	737.5
Others	132.4	121.7	266.2	204.8	207.9
Cash & equivalent	165.9	222.5	318.0	727.5	752.2
TOTAL ASSETS	5,169.0	5,566.5	5,400.1	5,260.1	5,484.9
Share capital	336.0	336.0	336.0	336.0	336.0
Minority Interest	(1.6)	(1.8)	(2.9)	(2.6)	(1.8)
Reserves	2,457.6	2,530.1	2,448.3	2,410.7	2,438.4
TOTAL EQUITY	2,792.0	2,864.3	2,781.4	2,744.1	2,772.6
Non-current liabilities	1,013.7	974.2	985.1	923.7	893.7
Long-term borrowings	818.7	747.6	748.1	728.7	698.7
Deferred tax liabilities	144.0	168.2	161.2	144.0	144.0
Others	51.1	58.3	75.8	51.1	51.1
Current liabilities	1,363.2	1,728.1	1,633.6	1,592.2	1,805.1
Short-term borrowings	670.8	1,059.7	1,029.7	1,000.0	1,200.0
Payables	677.6	652.4	592.1	577.4	590.3
Others	14.9	16.0	11.8	14.9	14.9
TOTAL LIABILITIES	2,376.9	2,702.2	2,618.8	2,516.0	2,698.9

Cash Flow Statement	FY15	FY16	FY17	FY18F	FY19F
Operating activities					
PBT	115.3	(15.1)	(111.6)	27.2	81.2
Depreciation & Amortization	133.3	131.2	140.4	141.1	141.8
Chgs in working capital	(424.6)	(95.9)	283.3	324.8	(177.5)
Interest expense	(52.8)	(66.1)	(65.1)	(60.5)	(66.5)
Tax paid	(54.4)	(6.1)	13.6	(6.4)	(19.9)
Others	65.7	(92.5)	3.4	57.9	64.4
CF from Operations	(217.5)	(144.5)	264.0	484.1	23.5
Investing activities					
Capex	(119.2)	(250.0)	(110.8)	(150.0)	(150.0)
Others	158.0	173.7	(120.8)	1.4	1.4
CF from Investments	38.8	(76.3)	(231.5)	(148.6)	(148.6)
Financing activities					
Dividends paid	(32.6)	(26.4)	(13.1)	(20.2)	(20.2)
Net proceeds in borrowings	25.7	301.2	79.8	(130.0)	170.0
Others	(0.6)	(0.0)	(0.3)	-	-
CF from Financing	(7.6)	274.8	66.5	(150.2)	149.8
Net changes in cash	(186.3)	54.0	98.9	185.3	24.8
Beginning cash	341.5	165.9	219.8	318.7	505.0
Overdrafts & Deposits	10.6	-	-	1.0	2.0
Ending cash	165.9	219.8	318.7	505.0	531.8
Ratios	FY15	FY16	FY17	FY18F	FY19F
Revenue growth	20.1%	-3.6%	-21.2%	10.8%	2.2%
EBIT growth	-19.4%	-88.9%	-200.1%	-473.9%	77.8%
Core net profit growth	-20.9%	-198.2%	50.6%	-123.2%	194.7%
PBT margin	2.0%	-0.8%	-1.7%	0.6%	1.7%
Core net profit margin	1.0%	-1.1%	-2.0%	0.4%	1.2%
ROE	1.2%	-1.1%	-1.6%	0.4%	1.1%
ROA	2.1%	-2.1%	-3.2%	0.7%	2.2%
Net gearing (%)	47.4%	55.3%	52.5%	36.5%	41.3%
Book value/share (RM)	4.15	4.26	4.14	4.08	4.13
PBV (x)	0.40	0.39	0.40	0.41	0.40
Interest Cover (x)	4.4	2.7	1.4	4.8	6.0
FCF (RMm)	(178.7)	(220.8)	32.4	335.5	(125.1)

DAILY PRICE CHART



Hafriz Hezry
hafriz.hezry@midf.com.my
03-2173 8392

MIDF RESEARCH is part of MIDF Amanah Investment Bank Berhad (23878 - X).

(Bank Pelaburan)

(A Participating Organisation of Bursa Malaysia Securities Berhad)

DISCLOSURES AND DISCLAIMER

This report has been prepared by MIDF AMANAH INVESTMENT BANK BERHAD (23878-X). It is for distribution only under such circumstances as may be permitted by applicable law.

Readers should be fully aware that this report is for information purposes only. The opinions contained in this report are based on information obtained or derived from sources that we believe are reliable. MIDF AMANAH INVESTMENT BANK BERHAD makes no representation or warranty, expressed or implied, as to the accuracy, completeness or reliability of the information contained therein and it should not be relied upon as such.

This report is not, and should not be construed as, an offer to buy or sell any securities or other financial instruments. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. All opinions and estimates are subject to change without notice. The research analysts will initiate, update and cease coverage solely at the discretion of MIDF AMANAH INVESTMENT BANK BERHAD.

The directors, employees and representatives of MIDF AMANAH INVESTMENT BANK BERHAD may have interest in any of the securities mentioned and may benefit from the information herein. Members of the MIDF Group and their affiliates may provide services to any company and affiliates of such companies whose securities are mentioned herein. This document may not be reproduced, distributed or published in any form or for any purpose.

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.