

28 February 2018 | 4Q17 Result Review

Tan Chong Motor


Turnaround potential grossly underestimated

- **4Q17 losses narrows significantly, ahead of expectations**
- **Inventories reduced to just above RM1b (-55%yoy)**
- **Best proxy to stronger RM, consensus grossly underestimating Tan Chong's earnings turnaround potential**
- **Contrarian BUY re-affirmed at unchanged TP of RM2.05**

Inflection point reached. Tan Chong's 4Q17 net loss narrowed significantly, at just RM7m and ended FY17 at a net loss of RM89m – the bulk of FY17 losses came in the earlier part of the year. The RM89m FY17 net loss was ahead of expectations accounting for 93% of our forecast losses and 95% of consensus.

EBITDA almost tripled, underpins our thesis. As we had alluded to and central to our BUY thesis on Tan Chong; the group benefits tremendously from the strong Ringgit. This is reflected in an almost tripling in EBITDA margins to 4.5% in 4Q17 against 3Q17. Similarly, EBITDA almost tripled in 4Q17 against flattish revenues. Unlike other major Japanese marques, Nissan TIV in 4Q17 was actually down 12%qoq while auto division revenues were actually flat qoq. The massive margin expansion was driven by: (1) Strong RM (2) Rollback in discounting (3) favourable model mix. Inventories gapped down to just above RM1b against the peak of RM2b in 1Q16.

Consensus underestimating Tan Chong's turnaround. Earnings should strengthen further in the next few quarters on the back of even stronger Ringgit levels (now ~RM3.90 vs. 4Q17: RM4.26). 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 the black in FY18 and to register more meaningful earnings in FY19F. Our forecasts however 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. As it is, our FY19F earnings is 27% above consensus, while for FY18F, consensus is still expecting a loss vs. our profit forecast of RM21m.

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 potential turnaround in earnings over the next few quarters. Key catalysts include: (1) Resumption of new model launch in FY18F (2) Sustained Ringgit strength (3) Further reduction in inventory levels. 

Maintain BUY
Unchanged Target Price: RM2.05

RETURN STATS

Price (27 Feb 2017)	RM1.71
Target Price	RM2.05
Expected Share Price Return	+19.9%
Expected Dividend Yield	+1.8%
Expected Total Return	+21.7%

STOCK INFO

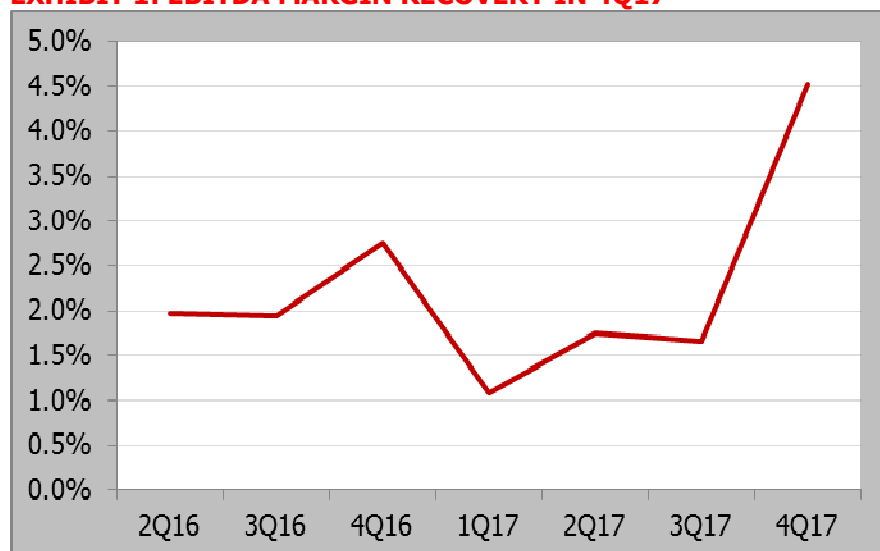
KLCI	1,871.46
Bursa / Bloomberg	4405 / TCM MK
Board / Sector	Main/Automotive
Syariah Compliant	Yes
Issued shares (mil)	652.66
Market cap. (RM'm)	1,116.05
Price over NA	0.40
52-wk price Range	RM1.29-1.95
Beta (against KLCI)	0.94x
3-mth Avg Daily Vol	0.21m
3-mth Avg Daily Value	RM0.35m
Major Shareholders (%)	
Tan Chong Consolidated	40.4
EPF	6.0
Nissan Motor	5.7

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)	19.2	(19.5)	(13.0)	56.0	19.0
Net Dividend (sen)	5.0	2.0	3.0	3.0	3.0
Net Dividend Yield (%)	2.9	1.2	1.8	1.8	1.8

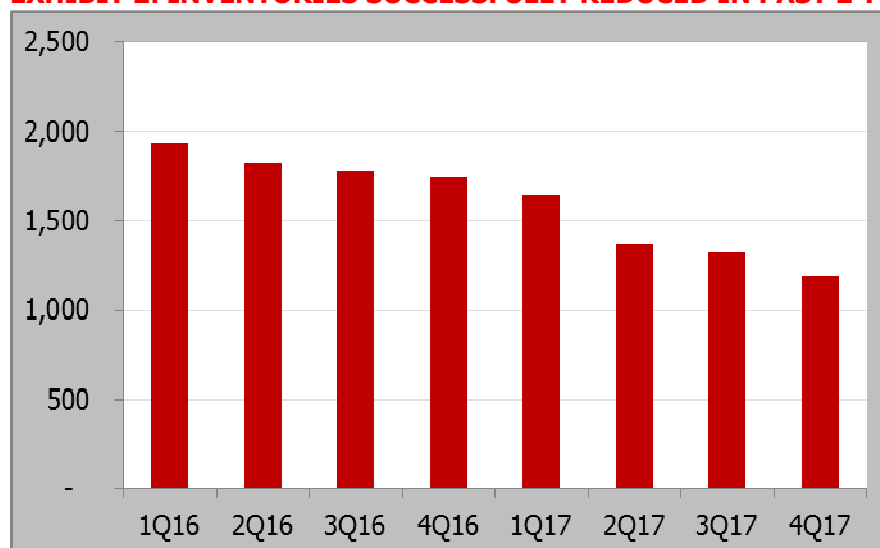
Source: Company, MIDF

EXHIBIT 1: EBITDA MARGIN RECOVERY IN 4Q17



Source: Company, MIDF

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



Source: Company, MIDF

EXHIBIT 1: TAN CHONG 4Q17 RESULT SUMMARY

YE Dec (RMmil)	4Q16	3Q17	4Q17	QoQ %	YoY %	FY16	FY17	YTD %
Revenue	1,273.0	1,073.3	1,076.0	0.3%	-15.5%	5,510.7	4341.2	-21.2%
Operating profit	24.9	(12.6)	27.1	NA	8.6%	18.7	(18.7)	-200.1%
Interest expense	(16.8)	(19.4)	(18.2)			(72.9)	(71.7)	-1.7%
Interest income	2.5	4.5	2.6			7.9	14.2	79.3%
Associates	0.8	0.4	1.1	160.3%	33.7%	3.2	3.4	4.7%
Pretax profit	11.4	(27.1)	12.6	-146.4%	10.3%	(43.1)	(72.8)	69.0%
Tax expense	(12.1)	0.4	(18.8)	-4320.4%	55.9%	(16.0)	(23.6)	47.8%
Minorities	(2.0)	(3.6)	1.0	-126.5%	-147.7%	(4.1)	(7.8)	90.5%
Net profit	1.4	(23.1)	(7.2)	-68.9%	-631.3%	(54.9)	(88.6)	61.3%
Core net profit	1.4	(23.1)	(7.2)	-68.9%	-631.3%	(58.8)	(88.6)	50.6%
EPS (sen)	0.2	(3.4)	(1.1)			(8.8)	(13.2)	
Gross DPS (sen)	1.00	0.00	1.00			2.00	2.00	
Operating margin (%)	2.0%	-1.2%	2.5%			0.3%	-0.4%	
Core operating margin (%)	3.1%	0.2%	3.9%			-0.7%	-1.7%	
Pretax profit margin (%)	0.9%	-2.5%	1.2%			-0.8%	-1.7%	
Net profit margin (%)	0.1%	-2.2%	-0.7%			-1.1%	-2.0%	
Tax rate (%)	-105.7%	-1.6%	-149.5%			37.0%	32.4%	
Total vehicles (units)	10,308	7,222	6,395	-11.5%	-38.0%	40,706	27,154	-33.3%
RM:USD (Spot, delayed by 3-mth)	4.05	4.33	4.26	-1.6%	5.2%	4.13	4.34	5.1%
Revenue/vehicle (RM000)	121.2	145.2	165.1	13.7%	36.2%	133.5	156.8	17.5%
Operating profit/vehicle (RM000)	2.4	-1.7	4.2	NA	75.0%	0.5	-0.7	N/A
Net profit/vehicle (RM000)	0.1	-3.2	-1.1	NA	-956.5%	-1.4	-3.3	N/A
Operating cost/vehicle (RM000)	121.1	150.4	164.0	9.1%	35.5%	134.9	160.6	19.0%

Source: Company, MIDF

EXHIBIT 2: TAN CHONG 4Q17 RESULT SUMMARY

YE Dec (RMmil)	4Q16	3Q17	4Q17	QoQ %	YoY %	FY16	FY17	QoQ %
Autos	1,249.1	1,048.5	1,055.7	1%	-15%	5,433.5	4,257.7	-22%
Financial Services	21.0	23.0	18.6	-19%	-11%	65.9	75.9	15%
Others	2.8	1.7	1.6	-7%	-43%	11.4	7.6	-33%
Total revenue	1,273.0	1,073.3	1,076.0	0%	-15%	5,510.7	4,341.2	-21%
Autos	34.6	17.4	47.8	175%	38%	101.4	96.5	-5%
Financial Services	9.6	5.1	5.5	8%	-42%	23.3	20.9	-10%
Others	15.5	(2.9)	(1.5)	-47%	-110%	34.0	(2.8)	-108%
Total EBITDA	59.6	19.6	51.9	164%	-13%	158.8	114.6	-28%
EBITDA margins								
Autos	2.8%	1.7%	4.5%			1.9%	2.3%	
Financial Services	45.8%	22.2%	29.7%			35.4%	27.5%	
Others	545.8%	-164.4%	-93.2%			298.8%	-36.9%	

Source: Company, MIDF

DAILY PRICE CHART



Source: Bloomberg, MIDFR

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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.