Indus Motor Company Limited
Move To Capture Market

BUY

Target Price (Jun-18)  2,204.6
Last Closing  1,712.3
Upside (%)  28.8
PSX Code INDU
Bloomberg Code INDUPA

Shares
Market Cap (USD m)  1,281.7
Outstanding Shares (m)  78.6
Free Float (%)  17.0
12M Avg. Daily Turnover (000)  40.46
12M High | Low (PKR)  1,973.0 | 1,357.0
Major Shareholders Toyota Corporation

Key Matrics
<table>
<thead>
<tr>
<th>FY17A</th>
<th>FY18F</th>
<th>FY19F</th>
</tr>
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<tbody>
<tr>
<td>Assets (PKR bn)  63.9</td>
<td>71.3</td>
<td>75.0</td>
</tr>
<tr>
<td>Equity (PKR bn)  31.2</td>
<td>35.8</td>
<td>40.5</td>
</tr>
<tr>
<td>PAT (PKR bn)  13.0</td>
<td>15.6</td>
<td>15.9</td>
</tr>
<tr>
<td>EPS (PKR)  165.4</td>
<td>198.4</td>
<td>201.7</td>
</tr>
<tr>
<td>P/E (x)  10.4</td>
<td>8.6</td>
<td>8.5</td>
</tr>
<tr>
<td>P/B (x)  4.3</td>
<td>3.8</td>
<td>3.3</td>
</tr>
<tr>
<td>DPS (PKR)  115.0</td>
<td>140.0</td>
<td>142.0</td>
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<tr>
<td>Div Yield (%)  6.7</td>
<td>8.2</td>
<td>8.3</td>
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<tr>
<td>ROE (%)  44.2</td>
<td>46.6</td>
<td>41.6</td>
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Stock Performance

Source: Bloomberg

Plan to Regain Lost Spot
Albeit, strong management and ability to reinvest in the business amid availability of ample liquidity remains a key to sustainable growth. In FY17, INDU sales recorded at 59.9K units, down by 6% YoY compared to 63.9K units in FY16. This translates into a reduction in market share from 29% to 28% given waning demand of 10th generation Corolla and heavy competition faced due to launch of Honda Civic. While in 2M FY18, total sales clocked-in at 10.2K units, up by 6% YoY. The company made a strong comeback to regain its lost share by launching 2nd generation Fortuner and 11th generation Toyota Corolla which revived the consumer’s interest active in the company; case in point: INDU enjoyed highest brand equity compared to peers and commenced delivery of face lifted Corolla with an order book reserved for all variants varying from Jan’18 to Mar’18. This was also evident from Corolla sales for the month Aug’17 at 4.8K units, up by 23% MoM in contrast to 3.9K units in Jul’17.

Upsward Revision of TP and Earnings
After incorporating the latest available financials released by the company for FY17, we revise upwards our Jun’18 DCF-based target price of Indus Motor Company Limited (INDU) to PKR 2,205/share (previously PKR 2,198/share). As the scrip provides a lucrative upside of 29% from last closing, we reiterate ‘BUY’ stance on the scrip. The earnings revision stems from i) change in sales mix; anticipation of higher sales of Fortuner (second generation) in the current year given overwhelming response to new model surpassing all the hopes and revising down our assumption of Hilux REVO sales, and ii) change in our margin assumption attributed to increase in prices. Pertinently, the stock has corrected by ~14% from its all-time high market rate of PKR 2,044/share, as FY18E / FY19F multiple eases to 8.6x / 8.5x.

Exhibit: Old & New Estimates

<table>
<thead>
<tr>
<th></th>
<th>FY18E</th>
<th>FY19F</th>
<th>Jun-18</th>
</tr>
</thead>
<tbody>
<tr>
<td>Target Price (PKR/Share)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Old</td>
<td>193.9</td>
<td>197.1</td>
<td></td>
</tr>
<tr>
<td>New</td>
<td>198.4</td>
<td>201.7</td>
<td></td>
</tr>
<tr>
<td>Change</td>
<td>2.3%</td>
<td>2.3%</td>
<td></td>
</tr>
<tr>
<td>EPS</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Old</td>
<td>135</td>
<td>140</td>
<td></td>
</tr>
<tr>
<td>New</td>
<td>140</td>
<td>142</td>
<td></td>
</tr>
<tr>
<td>Change</td>
<td>3.7%</td>
<td>1.4%</td>
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Source: AHL Research

Exhibit: Corolla Units Sold

Source: PAMA, AHL Research

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Fortuner sales on the other hand, were set at 535 units in 2MFY18 vis-à-vis 111 units in 2MFY17. Since launch of second generation of the new Fortuner model (Dec’16), sales have exhibited an enormous growth, as shown in the graph below. This elegant new model may corroborate Indus to regain its lost spot with growing share in total sales of the company. In FY17, Fortuner contributed 2% to total volumes, we anticipate Fortuner’s share to go up to ~4% in FY18E. Moreover, company has a robust demand of Fortuner with advance bookings in place till Dec’17, we expect sales to portray a similar trend as exhibited in 2MFY18.

**Exhibit: Fortuner Units Sold**

To recall, Hilux Vigo was replaced by the eight generation Hilux Revo; since launch in Nov’16 sales have to picked pace but due to production limitation, the company settled with sales of 5,860 units in FY17, down by 1% compared to 5,923 units in FY16. Revo faces no competition from local peers due to its uniqueness, quality and reliability. That said, orders have been reserved for the next 3 months (till Dec’17).

**Exhibit: Hilux Units Sold**

**Depreciation Risk to Overcome**

Risk of PKR depreciation is hovering around given rising current account deficit. As per management, INDU holds a strong presence in the market and with robust demand, the company will swiftly pass on the impact of any depreciation beyond PKR107/USD by increasing the retail prices of its vehicles.
Ample Capacity

Recently, INDU held an analyst briefing where the management revealed that debottlenecking of the paint shop will be complete by 3QFY18, while we anticipate the impact of expansion may be visible from FY19 and onwards. To recall, management has no plan to enhance more capacity other than ongoing debottlenecking of paint shop which will take capacity from 54.8k to 65.0k (without overtime).

Exhibit: Capacity Utilization

[Graph showing capacity utilization from FY13A to FY17A]

Source: Company Financials, AHL Research

Trading Sales Shelter Gross Margins

In FY17, gross margins of the company registered a growth of 135bps against SPLY, to be set at 17.7%. Reasons for increase in gross margins were i) increase in selling prices resulting in improved manufacturing margins to 16.2% vis-à-vis 15.4% in FY16, ii) augmented trading sales of completely built up (CBU) units (up by 142% to 5,547 units vs. 2,293 units in FY16 owed to rising interest in luxury vehicles and introduction of new models in passenger car and Sports Utility Vehicles category - Prius / Land Cruiser) whereby margins clocked-in at 36.1% in FY17 as opposed to 34.1% in FY16, and iii) stable PKR/USD in the said year.
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Equity Research Ratings

Arif Habib Limited (AHL) uses three rating categories, depending upon return form current market price, with Target period as December 2017 for Target Price. In addition, return excludes all type of taxes. For more details kindly refer the following table:

<table>
<thead>
<tr>
<th>Rating</th>
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<tbody>
<tr>
<td>BUY</td>
<td>Upside* of subject security(ies) is more than +10% from last closing of market price(s)</td>
</tr>
<tr>
<td>HOLD</td>
<td>Upside* of subject security(ies) is between -10% and +10% from last closing of market price(s)</td>
</tr>
<tr>
<td>SELL</td>
<td>Upside* of subject security(ies) is less than -10% from last closing of market price(s)</td>
</tr>
</tbody>
</table>

* Upside for Power Generation Companies (Ex. KEL) is upside plus dividend yield.

Equity Valuation Methodology

AHL Research uses the following valuation technique(s) to arrive at the period end target prices:

- Discounted Cash Flow (DCF)
- Dividend Discount Model (DDM)
- Sum of the Parts (SoTP)
- Justified Price to Book (JPTB)
- Reserved Base Valuation (RBV)

Risks

The following risks may potentially impact our valuations of subject security (ies):

- Market risk
- Interest Rate Risk
- Exchange Rate (Currency) Risk

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