

# KARSN.IS Karsan Otomotiv

MARKETPERFORM

RESEARCH DEPARTMENT

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## Reason of the Report

Company visit note

## General Company Information

Sector: Automotive & Parts

## Shareholder Structure

52.20%	Kiraca Automotive and Trade
33.03%	Other
12.52%	Diniz Group
2.25%	Inan Kirac
0.95%	Otoyl Sanayi AS

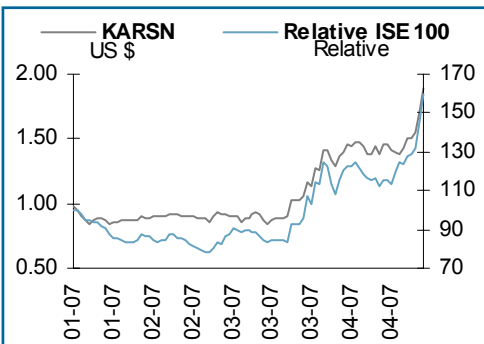
Stock Data	TRY	US \$
Share Price	2.54	1.90 \$
ISE-100	40,683	2.81 ¢
Number of Shares	100 mn	
Float	78%	
Market Cap.	254 mn	190 mn

Estimated Value	TRY	US\$
Target Mcap	287 mn	186 mn
Target Share Price	2.87 YTL	1.86 \$

Stock Performance	1 Mn	3 Mn	12 Mn
TL % Change	35.8	98.3	14.3
US\$ % Change	39.2	108.0	15.3
Rel.Index % Change	38.3	83.3	10.6
Average Volume mn\$	8.4	5.17	1.98

Stock Performance	1 Mn	12 Mn	YTD
Share Price Minimum (\$)	1.38	0.73	0.84
Share Price Maximum (\$)	1.90	1.90	1.90

Date	Cash Div.(mn\$)	Dividend Yield
31/05/2000	3.1	1.1%



**Could be one of the best growth stories at ISE...**

**How much of it is in the price ?**

Karsan's long time efforts to fully utilize its capacity as a contract manufacturer, started to give fruits. In February, the company signed a five year exclusive distribution agreement with Iran's Sanat Khuodro Kamau to export J9 midibus model to Iran, around 3,000 units p.a. This was followed by a 5 year contract with Hyundai to produce and distribute HD series trucks, 2,000 units, estimated to contribute \$35m/ p.a. And very recently, the company signed an MOU with Renault Trucks to produce trucks over 7.5 tonne weight, estimated to contribute €200m revenues with an annual 5,000 units of production. Finally, the company is a strong candidate to produce Partner's end of series model for Peugeot, which will mainly be exported to emerging countries, generating an additional 30,000 units of exports in 2009. Apart from these, the company is working on three new projects, which according to the company have 70% chance of materializing, increasing the production volume by another 13,500 units in 2009. Including all above mentioned projects, the company company gave a revenue guidance of \$596m and \$1.22 bn for 2008 and 2009, respectively, compared with \$190m in 2006. Apart from increase in sales volume, Karsan also projects its industrial sales to surge by 93% from \$16 mn in 2006 to \$31 mn in 2007. For 2008 and 2009, industrial sales are forecasted as \$50mn by the company.

Currently Karsan has a production capacity of 25,000 units. To raise the overall capacity to 58,000 units in three shifts, company requires an additional investment of only \$ 8 mn. Investments for the new projects will be carried out mostly by Renault and Hyundai.

Key Estimates (TRY mn)			
KARSN	2004	2005	2006
Sales	378	251	275
EBITDA	33	-3	16
Net Income	1.4	-47	-32
P/E	n.a	n.a	n.a
EV/EBITDA	9.46	n.a	9.53
EPS	0.01	-0.47	-0.32

COMPANY GUIDANCE	2006	2007e	2008e	2009e
<b>Domestic Sales (units)</b>	11,923	8,550	11,500	11,000
J-9	2,963	3,000	3,000	3,000
Partner	8,960	5,000	5,500	4,000
Hyundai HD35&HD75	0	550	2,000	2,000
Renault Trucks	0	0	1,000	2,000
<b>Export (units)</b>	394	7,750	20,500	59,500
J9	394	2,750	4,000	4,000
Partner	0	5,000	10,000	30,000
Renault Trucks	0	0	1,500	3,000
New Projects	0	0	5,000	22,500
<b>Total (units)</b>	<b>12,317</b>	<b>16,300</b>	<b>32,000</b>	<b>70,500</b>
<b>Turnover Vehicle</b>	\$173.5 mn	\$221.8 mn	\$545.9 mn	\$1,172.7 mn
<b>Turnover Industrial Sales</b>	\$16 mn	\$30.8 mn	\$50 mn	\$50 mn
<b>Total Turnover</b>	<b>\$189.5 mn</b>	<b>\$252.6 mn</b>	<b>\$595.6 mn</b>	<b>\$1,222.3mn</b>

Source : Company Presentation, May 2007

We have calculated below forward looking EV/EBITDA multiples for the company first by including already signed agreements only, including the Khuodro, Hyundai and Renault deals (please note that the company signed an MOU and the final agreement has not been signed yet), secondly by also adding Peugeot end of series project, and finally we have looked at the case where the company succeeds to finalize Peugeot end of series and three other new projects.

EV/EBITDA	2006	2007e	2008e	2009e
Signed agreements	15.6	11.2	5.9	4.6
Signed agreements + end of series Partner	15.6	9.7	5.1	3.4
Signed agreements + end of series Partner + new projects	15.6	9.7	4.5	2.4
Signed agreements +70% prob. For end of series Partner and ne	15.6	10.1	4.8	2.8

#### *IS Investment Estimates*

It seems that under all scenarios 2007 and 2008 expectations are already priced in. Here, we assume a target EV/EBITDA multiple of 4.5x for Karsan. However, the inclusion of end of series Partner project and three new projects lowers 09 E EV/EBITDA multiple to as low as 2.5x. Assuming a 70% probability for the new project and Partner exports, 09E EV/EBITDA multiple is 2.9x, implying an upside potential of 55%. Please note that contract manufacturing agreements of Karsan, where the brand owner carries most of the investments, are not on a take or pay basis, unlike Tofas' export agreements.

We set our fair market value for Karsan based on a target 4.5x 2009e EV/EBITDA multiple, including only the contribution from signed agreements. Thus, we currently rate the company as "MARKETPERFORM" with a target Mcap of \$186m. However, we might revise our target Mcap and recommendation when the new projects are firmed up.

#### **Karsan's New Projects**

- Life cycle of Partner is coming to an end in mid 2008 and Peugeot plans to produce Partner's end of series only for selling to emerging countries. Karsan is the most likely candidate for production of end of series Partners due to its capacity, experience and its proximity to export markets. Karsan aims to export 5,000 units Partners in 2007, 10,000 units in 2008 and 30,000 units in 2009. In 2005 and 2006 Karsan didn't export any Partners. This project is estimated to be finalized by June or September latest.

- Karsan signed a memorandum of understanding (MOU) with French truck producer Renault Trucks to produce trucks over 7.5 tonne weight. Final agreements parallel to MOU's principles are expected to be completed till the end of July, 2007. During this period, talks between the parties will continue. If the agreement is finalized, the trucks over 7.5 tonne weight will be produced in Turkey to be marketed in both Turkey and abroad. Total production number is forecasted at 5,000 units yearly. The production is expected to take start in mid 2008 and contribute an additional €200 mn to company's revenues. This project will have no effect on company's 2007 financials. A possible joint venture between Karsan and Renault trucks after three years is also being evaluated to strengthen the collaboration of two parties. Apart from this project, Karsan reported that their multi branded production strategy will continue.
- Company signed a 5-year agreement with Hyundai to produce and distribute the models of 3.5 ton and 7.5 ton weight capacity of HD series. Total production units is expected to be 2000 units per year, whereas the annual revenue generation of new project is forecasted as \$35 mn.
- Karsan signed a five year exclusive distribution agreement with Iran's Sanat Khodro Kamau to export J9 midibus model to Iran. J-9 Exports to Iran is expected to be around 3,000 units per year. In addition Khodro will also carry out the distribution of J-9 in Iraq, Afghanistan, Syria, Saudi Arabia, United Arab Emirates and CIS countries. Exports to these countries are expected to total 1,000 units / year.

KARSN	2004/12	2005/12	2006/12
<b>Balance Sheet KARSN (USDmn)</b>	<b>UFRS</b>	<b>UFRS</b>	<b>UFRS</b>
<b>Current Assets</b>	52	42	33
Cash and Cash Equivalents	0	0	0
Marketable Securities	0	0	0
Short-Term Trade Receivables	7	17	12
Other Short-Term Receivables	12	3	1
Inventories	32	20	19
Other Current Assets	1	1	0
Long Term Assets	90	80	69
Long-Term Trade Receivables	0	0	0
Other Long-Term Receivables	0	0	0
Long-Term Financial Assets	0	0	0
Tangible Fixed Assets	77	73	62
Intangible Fixed Assets	3	7	7
Other Long-Term Assets	10	0	0
Total Assets	141	121	102
Short Term Liabilities	46	23	19
Short-Term Financial Loans	27	14	7
Short-Term Trade Payables	9	6	7
Other Short-Term Payables	7	1	1
ST Advances Received	0	0	1
Other Short-Term Liabilities	3	1	2
Long Term Liabilities	17	55	49
Long-Term Financial Loans	16	55	48
Long-Term Trade Payables	0	0	0
Other Long-Term Payables	0	0	0
LT Advances Received	0	0	0
Other Long-Term Liabilities	1	1	1
Shareholders' Equity	78	43	33
Total Paid-in Capital	14	14	28
Adjustments to Share Capital	0	0	0
Premium in Excess of Par	4	4	4
Revaluation Funds	0	0	0
Reserves and Other Items	72	72	69
Current Year Income /(Losses)	1	-35	-23
Retained Earnings /(Acc. Losses)	-13	-12	-45
Total Liabilities and S.holders' Equity	141	121	102
<b>Income Statement KARSN (USDmn)</b>	<b>2004/12</b>	<b>2005/12</b>	<b>2006/12</b>
<b>Net Sales</b>	282	187	192
Cost Of Sales	-255	-183	-178
Service Revenues	0	0	0
Proceeds from Operations/int.+div+lease	0	0	0
GROSS PROFITS/LOSSES	27	4	14
Operating Expenses	-11	-14	-12
NET OPERATING PROFITS	16	-11	2
Income & Expenses From Other Operations	-7	-11	-7
Financial Expenses	-11	-5	-17
Net Changes on Monetary Positions	4	0	0
MINORITY INTERESTS	0	0	0
INCOME BEFORE TAXES	2	-27	-22
Taxation on Income	-1	-9	0
NET PROFIT AFTER TAXES	1	-35	-22
<b>Key Ratios</b>	<b>2004/12</b>	<b>2005/12</b>	<b>2006/12</b>
<b>Net Working Capital</b>	30	31	23
Net Cash	-44	-69	-55
Price to Book	0.60	1.09	1.41
EBITDA	24	-2	11
Gross Margin	9.6%	2.0%	7.1%
Operating Margin	5.7%	-5.7%	1.1%
EBITDA Margin	8.6%	-1.0%	5.8%
Net Margin	0.4%	-18.7%	-11.6%

KARSN	2004/12	2005/12	2006/12
<b>Balance Sheet KARSN (YTLmn)</b>			
<b>Current Assets</b>	69	56	46
Cash and Cash Equivalents	0	0	1
Marketable Securities	0	0	0
Short-Term Trade Receivables	9	23	16
Other Short-Term Receivables	16	4	2
Inventories	43	26	27
Other Current Assets	1	2	1
Long Term Assets	120	107	97
Long-Term Trade Receivables	0	0	0
Other Long-Term Receivables	0	0	0
Long-Term Financial Assets	0	0	0
Tangible Fixed Assets	104	98	87
Intangible Fixed Assets	4	9	9
Other Long-Term Assets	13	1	0
Total Assets	190	163	143
Short Term Liabilities	62	31	27
Short-Term Financial Loans	37	19	10
Short-Term Trade Payables	12	8	10
Other Short-Term Payables	10	2	2
ST Advances Received	0	0	1
Other Short-Term Liabilities	4	2	3
Long Term Liabilities	23	74	69
Long-Term Financial Loans	22	73	68
Long-Term Trade Payables	0	0	0
Other Long-Term Payables	0	0	0
LT Advances Received	0	0	0
Other Long-Term Liabilities	1	1	1
Shareholders' Equity	105	58	47
Total Paid-in Capital	19	19	40
Adjustments to Share Capital	0	0	0
Premium in Excess of Par	5	5	5
Revaluation Funds	0	0	0
Reserves and Other Items	97	97	97
Current Year Income /(Losses)	1	-47	-32
Retained Earnings /(Acc. Losses)	-18	-17	-64
Total Liabilities and S.holders' Equity	190	163	143
<b>Income Statement KARSN (YTLmn)</b>			
<b>Net Sales</b>	378	251	275
Cost Of Sales	-342	-246	-255
Service Revenues	0	0	0
Proceeds from Operations/int.+div+lease	0	0	0
GROSS PROFITS/LOSSES	36	5	19
Operating Expenses	-15	-19	-16
NET OPERATING PROFITS	22	-14	3
Income & Expenses From Other Operations	-10	-15	-10
Financial Expenses	-14	-6	-25
Net Changes on Monetary Positions	5	0	0
MINORITY INTERESTS	0	0	0
INCOME BEFORE TAXES	2	-36	-32
Taxation on Income	-1	-11	0
NET PROFIT AFTER TAXES	1	-47	-32
<b>Key Ratios</b>			
<b>Net Working Capital</b>	40	42	33
Net Cash	-58	-92	-78
Price to Book	2.38	4.31	5.32
EBITDA	33	-3	16
Gross Margin	9.64%	1.95%	7.06%
Operating Margin	5.71%	-5.74%	1.05%
EBITDA Margin	8.64%	-1.05%	5.80%
Net Margin	0.38%	-18.73%	-11.59%

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