

30 June 2010

Eco City Vehicles

Year End	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/08	19.0	(0.70)	(0.23)	0.00	N/A	N/A
12/09	24.7	(0.19)	(0.06)	0.00	N/A	N/A
12/10e	29.0	0.28	0.09	0.00	59.8	N/A
12/11e	32.0	0.80	0.26	0.00	20.7	N/A

Note: *PBT and EPS are normalised, excluding intangible amortisation and exceptional items.

Investment summary: Beginning to motor

Eco City Vehicles (ECV) is beginning to motor. Last year's revenues were up by 30%, with the promise of further strong growth in the current year. Management has strong ambitions both for the Mercedes Benz Vito taxi (Vito) and to extend into the hybrid commercial vehicle market. It is still too early to make confident medium-term predictions, but many of the signs seem to be pointing in the right direction.

Profits to be delivered in 2010

ECV delivered close to expectations in 2009, with revenues up by 30% to £24.7m and underlying pre-tax losses reduced by more than £0.5m. Sales of the Vito taxi hit internal targets, while there were useful developments in the downstream used vehicle, parts and aftermarket businesses. On the basis of the first four months' registrations, we are optimistic that the group will be profitable in the current year.

Medium-term potential

As the number of Vito taxis in the market rises, opportunities for the group's downstream activities will continue to improve. While the timetable to achieve optimum performance is significantly longer than for franchise car dealers, the income stream ought to prove more secure. The relationship with Mercedes Benz appears to be strengthening, as indicated by the progress being achieved on the commercial vehicle project, but looks essential in the immediate future to management delivering on its medium-term objectives.

Borrowings reduced

Net borrowings were reduced from £3.1m to £2.4m, with the taxi business set to be cash generative over the next two years. However, the group capital base is low and we would reiterate the possible need for additional long-term funding before long.

Valuation: Rating looking to the future

It is not yet appropriate to compare the prospective rating with that of other motor distributors. The group offers exciting medium-term potential, which could justify a somewhat higher share price, but several hurdles still need to be negotiated.

Price 5.38p
Market Cap £16m

Share price graph



Share details

Code ECV
Listing AIM
Sector Retailers (Automotive)
Shares in issue 302m

Price

52 week High 7.13p Low 2.75p

Balance Sheet as at 31 December 2009

Debt/Equity (%) 444
NAV per share (p) 0.2
Net borrowings (£m) 2.4

Business

ECV has exclusive UK distribution rights for the Mercedes Benz Vito taxi and is looking to extend the business into electrically operated light commercial vehicles.

Valuation

	2009	2010e	2011e
P/E Relative	N/A	N/A	253%
P/CF	1.2	1.4	1.0
EV/Sales	0.8	0.6	0.5
ROE	N/A	15%	20%

Geography based on revenues (2009)

	UK	Europe	US	Other
100%	0%	0%	0%	0%

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In line with expectations

ECV's results for the year to December 2009 were largely in line with City expectations, with underlying operating losses greatly reduced, as sales of the new Vito taxi began to accelerate. With the tough trading climate continuing and the renegotiation of banking terms, we have lowered our current year estimate, but the group shows every sign of delivering progressively improving returns into the future.

Heading towards profitability

With revenues ahead by 30%, the group got close to break-even in 2009, reducing underlying pre-tax losses by £0.52m to £0.19m. Equally significant was the acceptance in the market place of the Mercedes Benz Vito taxi, which has achieved a 24% share since its launch in the London market. On the basis of further sales progress in a challenging market so far in 2010, we expect to see a return to profit during the current year.

Exhibit 1: Revenue breakdown

	2008 £m	2009 £m	Change %
New vehicles	10.39	14.50	+40%
Used vehicles	1.84	4.02	+118%
Parts	2.47	2.94	+19%
Aftermarket	4.11	3.21	-22%
Other	0.22	0.01	
	19.03	24.67	+30%

Source: Company announcements

New Vehicles – ECV delivered 398 new Vito taxis to the market in 2009, more than three times the 113 that were sold in 2008. Reflecting the change in the group emphasis, sales of LTI taxis fell from the 247 of 2008 to just 80 vehicles. In total, unit sales rose by a third from 360 to 478, in line with the target set in our report published in January. However, in the context of the challenging market, in which UK taxi registrations rose nominally from 2,079 to 2,088, this represented a highly encouraging performance, especially in the light of the heavy amount of discounting by market incumbent LTI. Gross margins on the Vito were considerably higher than those earned on the LTI vehicles.

The current year has started well for ECV. SMMT figures for the first four months show Vito registrations ahead by 16% to 148 vehicles, in a market that has risen by just 4%. Our target of 500 vehicles for the full year is beginning to look challenging, but there have been two very difficult trading spells, stemming initially from the poor weather in January and February, while April sales were adversely affected by the impact on airport activity caused by the Icelandic volcano eruption and uncertainty in the run up to the general election. The trading statement refers to production being stepped up to 12 vehicles per week, which is a clear indication of management optimism.

Used vehicles – Used vehicle sales were more than doubled from 145 to 308 units, with gross margins sharply higher, up from the nominal 0.8% level earned in 2008 to a much more acceptable 4.9%. The key factor in this respect was the number of LTI vehicles traded in against the sales of new Vito taxis and a steady firming up of used vehicle values, following the sharp reverses seen during the second half of 2008. We would expect the increasing sales of new Vito taxis to lead to a

further rise in the sale of trade-ins, suggesting a further useful result in the current year, although with values stabilising, margins may fall a little short of those earned in 2009.

Parts and service – There were mixed, but somewhat related, performances from parts and service. A 22% fall in aftermarket revenues stemmed, in part, from a shift in demand as many taxi operators responded to the recession by moving their service work to the smaller ‘under-the-arches’ operators; lower revenue streams mean that work can sometimes be carried out free of VAT. This, in turn, contributed to a 19% rise in parts revenues as the group supplied smaller local repair shops with increasing numbers of parts/spares. There was also useful new business in both areas associated with the Vito taxi. ECV management responded to the challenge, reducing the cost-base, so that the net result was sustained operating profits.

We expect this part of the business to grow consistently over the medium term, as more Vito taxis are sold with service packages; there will be competition for service work from franchised Mercedes Benz CV dealers, but with lower charge-out rates the group ought to retain a majority of the business. Meanwhile, the group has retained its LTI service and parts franchise for east London, following restructuring of the latter’s retail franchise base.

Low emission vehicles – Useful progress continues towards the introduction of electric vehicles to the London market. The all-electric Vito taxi prototype was unveiled earlier this year, generating considerable interest. However, the speed and extent of the take-up of the vehicle remains to be seen. Costs to the taxi driver are currently seen to be rather high, but local and national government support is also evident.

A similar comment applies to the Mercedes Benz commercial vehicle project. The group took delivery of a 3.5 tonne hybrid truck last year, which generated useful feedback. Current plans involve the imminent introduction of a 7.5 tonne vehicle. The potential is again quite considerable, but the timetable for revenues is currently difficult to gauge.

Finance

From the above comments, the group appears to be negotiating a successful route through the tough trading climate. Our current year targets suggest revenues rising by some 15-20%; the middle of this range would produce a turnover of £29m. With the benefit of operational gearing, the group should see a return to useful profits, although, with the underlying performance affected by challenging trading conditions and the renegotiation of lending facilities, we have decided to pare back our earlier pre-tax target. We now look for underlying pre-tax profits of £0.275m.

Net borrowings were reduced from £3.07m to £2.42m over the year, although gearing rose sharply to reflect the consolidation of underlying and exceptional debits; with shareholders’ funds of just £0.55m, gearing was 444%. On present indications, we expect the group to be operationally cash neutral in the current year, although as we indicated in our earlier report, the ambitious medium- and longer-term plans involving acquiring further shares in One80 and developing the commercial vehicle franchise would be better managed if the group were able to secure further equity funding.

Exhibit 2: Financials

PROFIT & LOSS	£'000s	2006	2007	2008	2009	2010e	2011e
Year end 31 December							
Revenue		27,268	41,893	19,026	24,672	29,000	32,000
Cost of Sales		(23,299)	(35,805)	(14,928)	(20,544)	(24,500)	(27,000)
Gross Profit		3,969	6,088	4,098	4,128	4,500	5,000
EBITDA		399	1,175	(395)	191	580	1,140
Operating Profit (before GW and except.)		275	1,044	(580)	72	460	1,000
Goodwill Amortisation		0	0	0	0	0	0
Exceptionals		(519)	(3,982)	(564)	(622)	(200)	0
Associate income		0	0	(90)	(40)	(25)	0
Operating Profit		(244)	(2,938)	(1,234)	(590)	235	1,000
Net Interest		(77)	254	(33)	(218)	(160)	(200)
Associates		0	0	(90)	(40)	(25)	0
Profit Before Tax (norm)		198	1,298	(703)	(186)	275	800
Profit Before Tax (FRS 3)		(321)	(2,684)	(1,267)	(808)	75	800
Tax		34	(6)	20	14	0	0
Profit After Tax (norm)		232	1,292	(683)	(172)	275	800
Profit After Tax (FRS3)		(287)	(2,690)	(1,247)	(794)	75	800
Average Number of Shares Outstanding (m)							
		240.0	252.4	302.1	302.1	302.1	303.1
EPS - normalised (p)		0.10	0.51	(0.23)	(0.06)	0.09	0.26
EPS - FRS 3 (p)		(0.12)	(1.07)	(0.41)	(0.26)	0.02	0.26
Gross Margin (%)		14.6%	14.5%	21.5%	16.7%	15.5%	15.6%
EBITDA Margin (%)		1.5%	2.8%	(2.1%)	0.8%	2.0%	3.6%
Operating Margin (before GW and except.) (%)		1.0%	2.5%	(3.0%)	0.3%	1.6%	3.1%
BALANCE SHEET							
Fixed Assets		429	3,471	3,947	3,686	3,716	3,726
Intangible Assets		0	0	0	0	0	0
Tangible Assets		429	2,516	2,837	2,616	2,646	2,656
Investment in associates		0	955	1,110	1,070	1,070	1,070
Current Assets		4,765	5,705	6,423	5,297	6,925	8,790
Stocks		1,099	2,527	4,228	2,689	3,461	4,019
Debtors		2,163	1,916	2,148	2,352	2,965	3,371
Cash		1,503	1,262	47	256	500	1,400
Current Liabilities		(2,679)	(6,550)	(8,996)	(8,417)	(7,246)	(8,321)
Creditors		(2,594)	(6,489)	(5,886)	(5,760)	(6,770)	(7,471)
Short term borrowings		(85)	(61)	(3,110)	(2,657)	(476)	(850)
Long Term Liabilities		(128)	(42)	(23)	(21)	(2,550)	(2,550)
Long term borrowings		(100)	(8)	(9)	(21)	(2,550)	(2,550)
Other long term liabilities		(28)	(34)	(14)	0	0	0
Net Assets		2,387	2,584	1,351	545	845	1,645
CASH FLOW							
Operating Cash Flow		937	754	(2,988)	1,311	206	876
Net Interest		(77)	254	(31)	(218)	(160)	(200)
Tax		(90)	0	0	0	0	0
Capex		1	(2,217)	(506)	(52)	(150)	(150)
Acquisitions/disposals		0	(955)	(245)	0	0	0
Financing		0	0	0	0	0	0
Dividends		(150)	(300)	0	0	0	0
Net Cash Flow		621	(2,464)	(3,770)	1,041	(104)	526
Opening net (debt)/cash		723	1,318	1,193	(3,072)	(2,422)	(2,526)
HP finance leases initiated		0	0	0	0	0	0
Other		(26)	2,339	(495)	(391)	0	0
Closing net (debt)/cash		1,318	1,193	(3,072)	(2,422)	(2,526)	(2,000)

Source: Edison Investment Research, Eco City Vehicles accounts

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